No. 90-333-CFX
Status: GRANTED

Title: Lampf Pleva Lipkind Prupis & Petigrow, Petitioner
v.
John Gilbertson, et al.

Docketed:
August 10, 1990

Court: United States Court of Appeals
for the Ninth Circuit

Counsel for petitioner: Wilson,Stephen Joel, Turi,Leonard F., Olson,Theodore B.

Counsel for respondent: Allen,F. Gordon, Novack,Kenneth M., Batchelor,Jeffrey M., Rosenbaum,Lois O., Dod,Barry W., Layton,Robert, Kennedy,Jack L., Hoffman,Jonathan M., Cardoni,Susan D., Allen,F. Gordon

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1	Aug 10 1990	G	Petition for writ of certiorari filed.
2	Sep 14 1990		Brief of respondents John Gilbertson, et al. in opposition filed.
3	Sep 14 1990		Supplemental brief of petitioner Lampf Pleva, etc. filed.
4	Sep 19 1990		DISTRIBUTED. October 5, 1990
5	Oct 9 1990		Petition GRANTED. Justice Souter OUT.
			**********
7	Oct 19 1990		Order extending time to file brief of petitioner on the merits until December 5, 1990.
8	Dec 5 1990		Brief of respondents Comdisco, Inc., & Pontikes in support of petition filed.
10	Dec 5 1990		Brief of petitioner Lampf, Pleva, Lipkind, Prupis, & Petigrow filed.
11	Dec 5 1990		Joint appendix filed.
12	Dec 5 1990		Brief amici curiae of Arthur Andersen & Col, et al. filed.
13	Dec 5 1990		Brief amicus curiae of Securities Industry Assn. filed.
14	Dec 5 1990		Brief amicus curiae of Securities and Exchange Commission filed.
15	Dec 5 1990		Brief amicus curiae of American Council of Life Insurance filed.
9	Dec 6 1990		Record filed.
		*	Certified copy of original record and proceedings received. (2 Boxes).
16	Dec 17 1990		SET FOR ARGUMENT TUESDAY, FEBRUARY 19, 1991. (2ND CASE)
18	Dec 17 1990		Order extending time to file brief of respondent on the merits until January 14, 1991.
20	Jan 14 1991		Brief of respondents John Gilbertson, et al. filed.
21	Jan 14 1991		Brief amicus curiae of Bond Investors Association filed.
23	Jan 14 1991	X	Brief amicus curiae of Natl. Assn. of Securities and Commercial Law Attorneys filed.
19	Jan 15 1991		Lodging received. (10 copies).
22	Jan 17 1991		CIRCULATED.
24	Feb 11 1991	X	Reply brief of petitioner filed.
25	Feb 19 1991		ARGUED.

90-333

Supreme Court, U.S.
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No. 90-

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,
Petitioner,
VS.
JOHN GILBERTSON, JOHN V. REITZ, and
ANTHONY CATALAN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

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August 14, 1990

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QUESTIONS PRESENTED

This Court has recognized an implied private cause of action under section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)), and Rule 10b-5 (17 C.F.R. 240.10b-5) promulgated thereunder. However, this Court has never determined what shall be the statute of limitations applicable to such actions. The 1934 Act has several express causes of action, which are subject to express limitations periods. The question presented is:

1. Whether private civil actions for damages under section 10(b) and Rule 10b-5 shall be governed by a specific and uniform statute of limitations borrowed from the limitations periods applicable to express causes of action under the Securities Exchange Act of 1934 rather than being subject to limitations periods borrowed from the law of the state where the action happens to be filed?

LIST OF PARTIES

The following parties were Plaintiffs below and are Respondents before this Court:

Clifford B. Alterman, John Ball, Ruth Beecher, Theodore Beecher, Carolyn Beecher, Walter L. Beers, Robert E. Boekenoogen, Charles W. Botsford, Robert Callahan, Anthony E. Catalan, Bonnie J. Chambers as Conservator of the Estate of Robert W. Chambers, Joan Chatham, Ronald Chatham, Cliff Chulos, Perry Coleman, David Collier, Leo DePretto as Personal Representative of the Estate of Howard E. White, Arlyss D. Dunham, Jack E. Evans, Janice Gilbertson, John Gilbertson, Robert A. Graham, Harry E. Groth, Jr., William L. Gunnell, Woodrow Gwyn, Floyd E. Hambleton, Robert E. Johnson, Ronald Kirkilie, Judith MacDonald, Nickolas J. Madesh, Jerry E. Marks, H. Winston Marshall, Jay L. Maxwell,

Maxwell McDonald Investments, David McCullam, James R. McDonald, Ward E. Moore, Ethel Nunemacher, Howard H. Overback, Elman Peterson, Jr., Dale R. Peterson, Joseph C. Player, Deane E. Reimann, John V. Reitz, Earl D. Riddle, Harlan C. Selby, Bruce Sigman, Edith Trykar, Theodore Trykar, C. Wayne Warren, R. Mattison White, Paul Winklesky, Larry G. Zettle.

The following parties were Defendants below and are Respondents before this Court:

Alanthus Computer Corp., Alanthus Corp., Arnheim & McCostis, Anders G. Arnheim, Berlent Industries, Inc., Harvey N. Berlent, Buhler Software Services, Roald Buhler, Comdisco, Inc., Computer Value Associates, John M. Costello, James B. Cuthbert, Jerrold Feingold, Leonard Feingold, Edward G. Fizell, Global Computer Corp., Mark A. Hanson, Richard A. Heitmeyer, Robert M. Hurwitz, Jeflen Consulting Corp., Ronald Johnson, Martin S. Karnoff, Robert M. Kirby, Kirby Microprocessors, Inc., Kirby Computer Systems, Inc., Leasing Consultants Associates, Leasing Consultants, Inc., David G. Marks, Richard M. McCostis, William L. McKenna, P-Stat, Inc., Martin D. Pine, Kenneth M. Pontikes, Gordon S. Rosen Associates, Gordon S. Rosen, Noah Schreiber, Software Systems for Word Processors, Inc., Start Systems, Inc., Technical Marketing Services, Texcom Equipment Corp., Leonard F. Turi, William A. Ward, Robert A. Weber, Richard A. Wellbrock.

The following parties were third-party defendants below and are Respondents before this Court:

Wayne Hamersly, Sherman Kellar, Mack, Roberts, Hoyle & Co., Roger Nelson, Paulson Investment Co., James D. Quenemoen, Rockwood Computer Corp., Michael Welwood, R. G. Williams.

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OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,
Petitioner,
vs.
JOHN GILBERTSON, JOHN V. REITZ, and
ANTHONY CATALAN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

Petitioner Lampf, Pleva, Lipkind, Prupis & Petigrow respectfully prays that a writ of certiorari issue to review the judgment and decision of the United States Court of Appeals for the Ninth Circuit, filed February 20, 1990.

OPINIONS BELOW

The unpublished memorandum decision of the Court of Appeals for the Ninth Circuit is reprinted in Appendix B. Petitioner's timely petition for rehearing was denied by an unpublished order. (App. C) The unpublished opinion of the United States District Court for the District of Oregon (Redden, D.J.) is reprinted at Appendix D.

JURISDICTION

The Court of Appeals' order denying Petitioner's timely petition for rehearing was filed on May 16, 1990. (App. C.) Petitioner's motion to stay issuance of the mandate was denied by order filed June 20, 1990. Mandate was issued July 13, 1990. Jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

The pertinent provisions of the Securities Exchange Act of 1934 are set forth in Appendix A to this Petition.

STATEMENT OF THE CASE

Factual Background

Respondents include investors who purchased units in one or more of seven similar limited partnerships in 1979, 1980, and 1981.[1] Each limited partnership was described in an "Investment Memorandum" provided to potential investors. Petitioner Lampf, Pleva, Lipkind, Prupis & Petigrow ("Lampf") is a law firm located in West Orange, New Jersey, that allegedly assisted in the preparation of the investment memoranda.

Each limited partnership was created for the purpose of purchasing, and then leasing, computer equipment and certain computer software unrelated to the computer equipment. Each partnership had the potential to generate profits for the limited partners as well as attractive tax benefits.

[1]The partnerships were named: Duval Associates, Lamar Associates, Salem Associates, Columbia Associates, Mt. Hood Associates, Euston Associates, and Troy Associates.

All seven partnerships were complete economic failures, primarily because the partnerships failed to successfully market their computer software. During 1981-84 the limited partners and their general partners were repeatedly notified of facts demonstrating the partnerships' failures.

Despite the partnerships' woeful performances, the investors did not investigate the reasons for the partnerships' poor performance until 1986 when the Internal Revenue Service began disallowing the investors' tax benefits. The investors allege that at that point — five to seven years after their initial investments — they finally investigated the failure of the investments and discovered their claims.

Proceedings in the District Court

The investors filed two separate lawsuits in November 1986, alleging federal claims under section 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78*j*(b)), and the Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§ 1961-1968.[2] A third suit was later filed by Respondent Anthony Catalan.[3] Because of the obvious statute of limitations issues, the District Court limited discovery to matters relevant to the statute of limitations.

In February 1988 Petitioner Lampf and other defendants below moved for summary judgment on the grounds that the investors had failed to commence their actions

[2]*John V. Reitz, et al. v. Leasing Consultants Associates, et al.*, District of Oregon Case No. 86-1368-RE; *John and Janice Gilbertson, et al., v. Leasing Consultants Associates, et al.*, District of Oregon Case No. 86-1369-RE.

[3]*Anthony E. Catalan v. Paulson Investment Company, et al.*, District of Oregon Case No. 87-593-RE.

within the time allowed by law. Petitioner Lampf raised the issue of whether the District Court should look to federal law for the limitations period applicable to section 10(b) rather than borrowing the limitations period from the law of the forum state.

In July 1988 the District Court issued a written opinion granting Petitioner's motion in all three cases. (App. D.) Following Ninth Circuit precedent, the District Court borrowed the statute of limitations from the law of the forum state (Oregon), and held that the investors' claims were time-barred because they failed to file suit within two years from when they were on inquiry notice of their potential claims. The District Court did not address Petitioner's argument that federal law should provide the limitations period for claims under section 10(b).

Proceedings Before the Court of Appeals

The investors in all three cases appealed to the United States Court of Appeals for the Ninth Circuit, arguing there were questions of fact that precluded summary judgment. In its brief to the Ninth Circuit, Petitioner Lampf again argued that federal law — and specifically the Securities Exchange Act of 1934 — rather than state law should provide the statute of limitations for section 10(b).

The issue of the applicable statute of limitations was important because if the court looked to federal law, an absolute three-year limitations period would apply. All investors' securities claims would be indisputably time barred because all investors purchased their limited partnership interests at least five years before filing suit.

On February 5, 1990 the Ninth Circuit issued a single memorandum decision reversing the District Court's judgments on the grounds there were questions of fact

whether the investors had actual or inquiry notice of their claims more than two years before commencing their actions. (App. B.) The Ninth Circuit followed existing precedent and looked to the law of the forum state for the applicable statute of limitations. The court did not respond to Petitioner's argument that federal law should provide the limitations period.

Petitioner filed a timely petition for rehearing and suggestion for rehearing en banc. The petition for rehearing raised several issues, including the question of the applicable statute of limitations. On May 16 the petition was denied and the suggestion for hearing en banc was rejected. (App. C.)

REASONS FOR GRANTING THE WRIT

I.

THERE IS A CONFLICT AMONG AND WITHIN THE CIRCUITS REGARDING THE STATUTE OF LIMITATIONS APPLICABLE TO ACTIONS UNDER SECTION 10(b) AND RULE 10b-5

The circuit courts of appeal are divided over whether state or federal law should provide the statute of limitations for section 10(b) actions. Furthermore, conflicts are developing *within* some circuits. This Court should grant the writ of certiorari in order to resolve these conflicts.

The Third Circuit has held that federal law shall provide the limitations period for section 10(b) claims. In *In Re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.) (en banc), *cert. denied*, ___ U.S. ___, 109 S. Ct. 131, 102 L.Ed.2d 103 (1988) the court held that actions under section 10(b) are subject to the limitations period that applies to express actions under the 1934 Act. Claims expressly provided for in the 1934 Act must be

filed one year from discovery of the claim and no more than three years from the date of the violation. 15 U.S.C. §§ 78*i*(e), 78*r*(c), 78*cc*(b).

The Third Circuit's holding relied on this Court's decisions in *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987) and *Del Costello v. Teamsters*, 462 U.S. 151 (1983), where this Court indicated that lower courts should reconsider their predilection for looking to state law to find limitations periods for federal actions.

The two circuits that have addressed the issue after *Data Access* have declined to follow the *Data Access* approach. The Ninth and Eleventh Circuits have held recently that they will continue to look to state law for the applicable statute of limitations. *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990); *Smith v. Duff and Phelps, Inc.*, 891 F.2d 1567, 1569-70 (11th Cir. 1990).[4] Thus, there is a clear conflict between the Third, Ninth, and Eleventh Circuits.

There is a further conflict between the Third Circuit and other circuits that have traditionally looked to state law for the statute of limitations, but which have not revisited the issue since *Data Access*. Each of the following circuits holds that the limitations period for section 10(b) claims should be borrowed from state law:

FIRST CIRCUIT: *Maggio v. Gerard Freezer & Ice Co.*, 824 F.2d 123, 124 (1st Cir. 1987); *In Re Atlantic Financial Management, Inc. Securities Litigation*, 718 F. Supp. 1003, 1010 (D. Mass. 1988).

[4]In this case the Ninth Circuit ignored the issue entirely.

SECOND CIRCUIT: *Armstrong v. McAlpin*, 699 F.2d 79, 86 (2d Cir. 1983); *Azurite Corp. Ltd. v. Amster & Co.*, 730 F. Supp. 571, 582 (S.D.N.Y. 1990).

FOURTH CIRCUIT: *Gurley v. Documation, Inc.*, 674 F.2d 253, 258 (4th Cir. 1982).

FIFTH CIRCUIT: *Jensen v. Snellings*, 841 F.2d 600, 606 (5th Cir. 1988).

SIXTH CIRCUIT: *Silverberg v. Thomson McKinnon Securities, Inc.*, 787 F.2d 1079, 1081-82 (6th Cir. 1986); *Nichols v. Merrill Lynch, Pierce, Fenner & Smith*, 706 F. Supp. 1309, 1335 (M.D. Tenn. 1989).

SEVENTH CIRCUIT: *Norris v. Wirtz*, 818 F.2d 1329, 1333 (7th Cir.), *cert. denied*, 484 U.S. 943 (1987).

EIGHTH CIRCUIT: *Vanderboom v. Sexton*, 422 F.2d 1233 (8th Cir.), *cert. denied*, 400 U.S. 852 (1970); *Dingler v. T.J. Raney & Sons, Inc.*, 708 F. Supp. 1044, 1053-55 (W.D. Ark. 1989).

TENTH CIRCUIT: *Loveridge v. Dreagoux*, 678 F.2d 870, 874 (10th Cir. 1982); *Marchese v. Nelson*, 700 F. Supp. 522, 524 (D. Utah 1988).

D.C. CIRCUIT: *Forrestal Village, Inc. v. Graham*, 551 F.2d 411, 413 (D.C. Cir. 1977).

In addition to the conflict *among* the circuits, splits are emerging *within* some circuits. District courts in the Second, Seventh, Eighth, and Eleventh Circuits have rejected existing circuit precedent and adopted the *Data Access* rule. *Welch v. Cadre Capital*, 735 F. Supp. 467, 480-82 (D. Conn. 1989); *Robertson v. Deloitte, Haskins & Sells*, 732 F. Supp. 979, 984-85 (E.D. Ark. 1990); *Bath v. Bushkin, Gaims, Gaines & Jonas*, 695 F. Supp. 1156, 1159-62 (D. Wyo. 1988); *Bernstein v. Crazy Eddie, Inc.*, 702 F.

Supp. 962, 981 (E.D.N.Y. 1988); *Kayne v. PaineWebber, Inc.*, 703 F. Supp. 1334, 1343 (N.D. Ill. 1989).

In summary, there is a conflict *among* the circuits and *within* the circuits. Only this Court can bring peace to this chaotic situation, which will become more chaotic and unpredictable with the passage of time. Accordingly, the writ of certiorari should be granted.

II.

IT IS OF VITAL PUBLIC IMPORTANCE THAT THIS COURT BRING CERTAINTY, PREDICTABILITY, AND UNIFORMITY TO THE FIELD OF SECURITIES LAW BY DECIDING THE LIMITATIONS PERIOD APPLICABLE TO SECTION 10(b) ACTIONS

There are few matters in the law more important or more beneficial than certainty, predictability, and uniformity in statutes of limitations. Although these benefits are clear, there is no certainty, predictability, or uniformity regarding the limitations period for section 10(b) claims. Instead, it is an area of confusion and uncertainty, with courts unable to even agree on whether federal or state law should be the source of the statute of limitations. This Court should grant the writ of certiorari in order to bring certainty and uniformity to this important question of federal law.

A certain, predictable, and uniform statute of limitations is fundamental to any cause of action. This is particularly true of securities claims. Fairness dictates that investors know with reasonable certainty the maximum amount of time available to file claims arising from securities violations. Similarly, persons participating in the sale of securities need clear and uniform standards by which they can judge when their exposure to securities

claims is ended. Uncertainty serves neither the buyer nor the seller of securities.

The courts also need certainty and uniformity. Currently, the statute of limitations is an issue in virtually every securities case because the litigants do not know what limitations period will be applied by the district court. Counsel for defendants have the right and duty to argue for the shortest possible limitations period. Counsel for plaintiffs support the longest plausible time period. Therefore, district courts are forced to not only decide *whether* a claim is time-barred, but must also make the threshold determination of *what* limitations period applies. *See, e.g., Levy v. Eletr,* 724 F. Supp. 1269, 1270-72 (N.D. Cal. 1989); *Hempel v. Blunt, Ellis & Loewi, Inc.,* 123 F.R.D. 313, 315 (E.D. Wisc. 1988). This unproductive and time consuming waste of judicial resources could be completely eliminated if this Court were to resolve the issue of the applicable statute of limitations.

Uniformity must be a primary consideration in deciding upon the applicable limitations period. Currently, except in the Third Circuit, different limitations periods apply in each state. For example, a claim filed in the state of Oregon is subject to a two-year statute of limitations, while an action filed in the state of Washington is subject to a three year limitations period. *Nesbit,* 896 F.2d at 384 (applying two-year statute of limitations borrowed from Oregon law); *Reeves v. Teuscher,* 881 F.2d 1495, 1501 (9th Cir. 1989) (applying three-year statute of limitations borrowed from Washington law). More bizarre, claims filed in different federal districts in the *same* state can be subject to *different* limitations periods. For example, a 10(b) claim filed in the *Eastern* District of Arkansas is subject to a one-year-from-discovery/three-years-from-violation limitations period borrowed from the 1934 Act.

Robertson, 732 F. Supp. at 984-85. However, an action filed in the *Western* District of Arkansas is governed by a different limitations period. *Dingler v. T. J. Raney & Sons, Inc.,* 708 F. Supp. 1044, 1054-55 (W.D. Ark. 1989) (applying five-year limitations period based on Arkansas law). Such a crazy patchwork quilt of limitations periods is unjustifiable.

Furthermore, the current framework encourages the disfavored practice of forum shopping. Plaintiffs who have sat on their rights can pick and choose among various forums until they find one with a generous statute of limitations. Under the liberal jurisdiction and venue provisions of the securities laws, defendants can be haled into court almost anywhere, regardless of how tenuous their connection with that jurisdiction.

The lack of uniformity is particularly inappropriate in the area of securities law. A typical securities transaction will touch on many states. A securities issuer in Oregon may work with an underwriter in New York, an attorney in California, an accountant in Illinois, and sell to investors in Texas, New Mexico, Florida, and Arizona. In this simple scenario, eight different limitations periods could apply to one transaction. Neither potential plaintiffs nor potential defendants can have any confidence regarding what limitations period will apply. Furthermore, a court confronted with claims arising from this transaction would have to waste an inordinate amount of time sifting through the laws of the various states to decide which statute or statutes of limitations to apply.

The lack of certainty, predictability, and uniformity arises from many courts' misguided practice of borrowing the limitations period from state law. This habit is completely unjustified in the securities field, which is a matter of particular federal interest and concern. Securities claims are a matter of such great federal interest that Congress has vested the federal courts with exclusive jurisdiction to hear claims arising under the Securities Exchange Act of 1934. 15 U.S.C. § 78*aa*. It is anomalous indeed for state law to provide the limitations period for claims subject to exclusive federal jurisdiction.

The tradition of looking to state law for the statute of limitations is particularly perplexing because Congress has not been silent regarding what limitations period should apply to securities law claims under the 1934 Act. Looking to state law is appropriate where Congress has provided no guidance, but the 1934 Act itself provides that claims under Sections 9, 18, and 29 are subject to the one-year-from-discovery/three-years-from-violation limitations period. 15 U.S.C. §§ 78*i*(e), 78*r*(c), 78*cc*(b). These provisions offer unmistakable guidance regarding Congress's view of what limitations period should apply to claims under the 1934 Act.

There is currently great confusion regarding the statute of limitations for section 10(b) claims. This Court can end this unnecessary and wasteful chaos by settling the question of what limitations period controls section 10(b) claims. That limitations period should be the one-year-from-discovery/three-years-from-violation rule set forth in the 1934 Act itself.

CONCLUSION

This Court should grant the writ of certiorari for the purpose of holding that claims under section 10(b) are subject to the express limitations periods contained in the Securities Exchange Act of 1934. Such a holding would require reversal of the decision of the Ninth Circuit because the investors in this case all purchased their

securities more than three years before filing suit against Petitioner.

Respectfully submitted,

BULLIVANT, HOUSER, BAILEY,
PENDERGRASS & HOFFMAN

By _____
Stephen Joel Wilson
R. Daniel Lindahl

Attorneys for Petitioner Lampf, Pleva, Lipkind, Prupis & Petigrow

APPENDIX A

Section 9(a), (b), (c), (e) of the Securities Exchange Act of 1934, 15 U.S.C. § 78*i*(a), (b), (c), (e):

(a) It shall be unlawful for any person, directly or indirectly, by the use of the mails or any means or instrumentality of interstate commerce, or of any facility of any national securities exchange, or for any member of a national securities exchange —

(1) For the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or a false or misleading appearance with respect to the market for any such security, (A) to effect any transaction in such security which involves no change in the beneficial ownership thereof, or (B) to enter an order or orders for the purchase of such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties, or (C) to enter any order or orders for the sale of any such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties, or (D) to enter any order or orders for the sale of any such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the purchase of such security, has been or will be entered by or for the same or different parties.

(2) To effect, alone or with one or more other persons, a series of transactions in any security registered on a

national securities exchange creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

(3) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination in the ordinary course of business of information to the effect that the price of any such security will or is likely to rise or fall because of market operations of any one or more persons conducted for the purpose of raising or depressing the prices of such security.

(4) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to make, regarding any security registered on a national securities exchange, for the purpose of inducing the purchase or sale of such security, any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact, and which he knew or had reasonable ground to believe was so false or misleading.

(5) For a consideration, received directly or indirectly from a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination of information to the effect that the price of any such security will or is likely to rise or fall because of the market operations of any one or more persons conducted for the purpose of raising or depressing the price of such security.

(6) To effect either alone or with one or more other persons any series of transactions for the purchase and/or sale of any security registered on a national securities exchange for the purpose of pegging, fixing, or stabilizing the price of such security in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * *

(b) It shall be unlawful for any person to effect, by use of any facility of a national securities exchange, in contravention of such rules and regulations as the commission may prescribe as necessary or appropriate in the public interest or for the protection of investors —

(1) any transaction in connection with any security whereby any party to such transaction acquires any put, call, straddle, or other option or privilege of buying the security from or selling the security to another without being bound to do so; or

(2) any transaction in connection with any security with relation to which he has, directly or indirectly, any interest in any such put, call, straddle, option, or privilege; or

(3) any transaction in any security for the account of any person who he has reason to believe has, and who actually has, directly or indirectly, any interest in any such put, call, straddle, option, or privilege with relation to such security.

* * *

(c) It shall be unlawful for any member of a national securities exchange directly or indirectly to endorse or guarantee the performance of any put, call, straddle, option, or privilege in relation to any security registered

on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * *

(e) Any person who willfully participates in any act or transaction in violation of subsections (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity in any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant. Every person who becomes liable to make any payment under this subsection may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment. No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78*j*(b):

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange —

* * *

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities

exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Section 18(a), (c) of the Securities Exchange Act of 1934, 15 U.S.C. § 78*r*(a), (c):

(a) Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78*o* of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

* * *

(c) No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause

of action and within three years after such cause of action accrued.

Section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78*cc*(b):

Every contract made in violation of any provision of this chapter or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this chapter or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, or regulation: *Provided*, (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 78*o* of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) or subsection (c) or section 78*o* of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

Rule 10b-5, 17 C.F.R. 240.10b-5:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

APPENDIX B

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JOHN v. REITZ; JUDITH MACDONALD; DALE R. PETERSON; EARL D. RIDDLE; JACK E. EVANS; HARLAN C. SELBY; ROBERT E. JOHNSEN; PERRY COLEMAN; NICKOLAS J. MADESH; ROBERT A. GRAHAM; JERRY E. MARKS, et al.,
Plaintiffs-Appellants,

v.

LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.; GLOBAL COMPUTER CORPORATION; RONALD JOHNSON; TEXCOM EQUIPMENT CORPORATION; COMDISCO, INC.; KENNETH M. PONTIKES; MARTIN KARNOFF; JOHN COSTELLO; DAVID MARKS; GORDON S. ROSEN ASSOCIATES, INC.; GORDON S. ROSEN; SOFTWARE SYSTEMS FOR WORD PROCESSORS, INC.; BERLENT INDUSTRIES, INC.; HARVEY BERLENT,
Defendants-Appellees.
No. 88-4077
D.C. Civ-86-1368-RE

MEMORANDUM*

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* This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except as provided by 9th Cir. Rule 36-3.

ANTHONY E. CATALAN,
Plaintiff-Appellant,

v.

PAULSON INVESTMENT COMPANY, INC.; LAMPF, PLEVA, LIPKIND; PRUPIS & PETIGROW; COMPUTER VALUE ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; TECHNICAL MARKETING SERVICES, INC.; LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.,
Defendants-Appellees.
No. 88-4099
D.C. CV-87-593-RE

JOHN GILBERTSON AND JANICE GILBERTSON, et al.,
Plaintiffs-Appellants,

v.

ANDERS G. ARNHEIM; ALANTHUS CORPORATION, formerly known as Technology Finance Group, Inc.; COMPUTER VALUE ASSOCIATES; AMERICAN COMPUTER EQUIPMENT LEASING; LEASING CONSULTANTS ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; WILLIAM MCKENNA; TEXCOM EQUIPMENT CORPORATION; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.,
Defendants-Appellees.
No. 88-4100
D.C. CV-86-1369-RE

Appeals from the United States District Court
for the District of Oregon
James A. Redden, District Judge, Presiding

Argued and Submitted September 12, 1989
Portland, Oregon

Before: PREGERSON, TROTT, and FERNANDEZ, Circuit Judges.

SUMMARY

Appellants, investors in limited partnerships, appeal summary judgment for appellees, creators and marketers of the partnerships, on the ground that statutes of limitation bar appellants' federal and state securities fraud claims.

We hold that questions of material fact remain as to whether appellants had inquiry notice and what knowledge the general partners possessed. We also hold that the statute of limitations period governing the federal securities fraud claims governs the federal RICO claims. Finally, we vacate dismissal of the pendent claims. Accordingly, we reverse and remand.

PROCEEDINGS BELOW

Most appellants filed complaints on November 3, 1986, alleging violations of: § 17(a)(1) of the Securities Act of 1933, 15 U.S.C. §§ 771 and 77g; § 10b of the Securities Exchange Act of 1934 and Rule 10b-5, 15 U.S.C. § 78j(b) and 17 C.F.R. § 240.10b-5, respectively; and federal RICO, 18 U.S.C. § 1961, *et seq.* Appellants also brought pendent state claims.

The district court found, as a matter of law, that time barred the federal claims because: (1) reports to

appellants of the drastic decline in value of their investments had put them on inquiry notice by fall 1982; (2) the general partners' knowledge in summer 1982 of allegations of fraud and the results of an investigation into them constituted inquiry notice that was imputed to appellants; and (3) distribution of the reports and installation of a general partner previously associated with appellees did not constitute fraudulent concealment tolling the statutes of limitations. The district court declined to exercise pendent jurisdiction over the remaining state claims.

STANDARD OF REVIEW

The circuit court reviews de novo the district court's grant of summary judgment. *Conmar Corp. v. Mitsui & Co. (U.S.A.), Inc.*, 858 F.2d 499, 501 (9th Cir. 1988), *cert. denied*, 109 S. Ct. 795 (1989). Summary judgment is appropriate only where no genuine issues of material fact exist, and the moving party is entitled to prevail as a matter of law. *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.*, 739 F.2d 1434, 1436 (9th Cir. 1984). The court must view the evidence in the light most favorable to the party opposing the motion. *Id.* "Because our precedent dictates that the question of notice of fraud is for the trier of fact, the party seeking summary disposition has an extremely difficult burden to show that there exists no issue of material fact regarding notice." *Admiralty Fund v. Hugh Johnson & Co.*, 677 F.2d 1301, 1309-10 (9th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983); *Volk v. D.A. Davidson & Co.*, 816 F.2d 1406, 1417 (9th Cir. 1987). Summary disposition on the ground of the statute of limitations is discouraged. Admiralty Fund, 677 F.2d at 1310. A court may grant summary judgment only "if the uncontroverted evidence irrefutably demonstrates that a plaintiff

discovered or should have discovered the fraud but failed to file a timely complaint." *Volk*, 816 F.2d at 1417.

ANALYSIS

I

Inquiry Notice

The analogous forum state statute of limitations period continues to govern § 10(b) claims. *Davis v. Birr, Wilson & Co., Inc.*, 839 F.2d 1369 (9th Cir. 1988) (applying analogous state limitations period despite concurrence urging application of analogous federal period). Therefore, Oregon's two-year fraud statute of limitations period governs all of the federal securities claims at bar. *Volk*, 816 F.2d at 1411-12. A four-year period governs the federal RICO claims. *Agency Holding Corp. v. Malley-Duff & Assocs.*, 483 U.S. 143 (1987). If appellants lacked inquiry notice of their federal securities claims by November 1984 (two years before most filed their complaints), then they also lacked inquiry notice of their federal RICO claims by November 1982. Accordingly, we focus upon the issue of whether appellants had inquiry notice of their federal securities claims by November 1984.[1]

Although state law governs the length of the limitations period for the federal securities claims, federal law

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[1]We need not decide whether the federal RICO limitations period begins, as *Volk* suggests, when a federal securities claim begins, or, as appellants urge, when a plaintiff knows or should know of the existence of the elements of an action or the last injury or predicate act occurring as part of the same racketeering activity. Because we hold that the limitations period had not run on appellants' federal securities claims when they filed, the period necessarily had not run on their RICO claims.

controls when the period starts. *Volk*, 816 F.2d at 1412. The statute of limitations (for § 10(b) of the 1934 Act (15 U.S.C. § 78j(b)) and § 17(a)(2)-(3) of the 1933 Act (15 U.S.C. § 77q)) starts upon "actual or inquiry notice that a fraudulent misrepresentation has been made." *Id.* Inquiry notice arises when plaintiff could discover the fraud through the exercise of reasonable diligence. *Id.* "[R]easonable diligence is tested by an objective standard." *Kramas v. Security Gas & Oil, Inc.*, 672 F.2d 766, 770 (9th Cir.), *cert. denied*, 459 U.S. 1035 (1982). Investors have inquiry notice of fraud when they "should discover that they paid an inflated price for securities as a result of misleading statements or omissions." *Id.* 1414.

We have reversed summary judgment and held that knowledge of an investment's failure does not necessarily constitute inquiry notice of fraud where nonfraudulent business events might explain the failure. *See, e.g., Admiralty Fund*, 677 F.2d at 1310 (9th Cir. 1982) (declining, dramatically fluctuating stock price did not yield inquiry notice, as a matter of law, that stock offering prospectus had misrepresented issuer's financial strength, because "[g]eneral market conditions, subsequent events, or the inherent risk of the business could have been responsible" for the stock changes); *Briskin v. Ernst & Ernst*, 589 F.2d 1363, 1368 (9th Cir. 1978) (knowledge of survivor company's post-merger financial problems — including private placement of stock at lower price than represented at time of merger, missed dividend, and 85% decline in common stock price — did not constitute inquiry notice, where "[m]arket evidence might point equally to a general decline in the economy or post-merger mismanagement as the cause of . . . [the survivor's] financial condition"); *see also Mosesian v. Peat, Marwick, Mitchell & Co.*, 727 F.2d 873, 878 (9th Cir.), *cert. denied*, 469 U.S. 932 (1984)

(reversing judgment notwithstanding the verdict in holding that knowledge of company's financial problems, including large, rapid decline in stock price, sudden losses, suspension of trading in stock, and difficulty with creditors, did not necessarily suggest accounting fraud, where problems could instead result from "financial mismanagement, cost overruns, general market conditions, or other events unrelated to accounting fraud").

Volk, holding that knowledge that coal mines lacked represented reserves constituted inquiry notice of fraud, is distinguishable. This knowledge necessarily suggested fraudulent misrepresentation of the reserves because the amount of coal was scientifically verifiable and unchangeable in a human timespan. The *Volk* investors knew not only that their investments had performed dramatically below projections, but also that the projections had been based upon facts objectively ascertainable at offering time and not subject to risk of subsequent change. In contrast, in the instant case, appellants' knowledge that the software investment had performed dramatically below projections did not necessarily suggest intentional misrepresentation of income projections, upon which the software appraisals were based, at offering time. Rather, the software failures could have resulted from realization of the risks of technological obsolescence, market change, and lessee marketing difficulties — of which the offering memoranda had warned and to which the Lawrence Reports (except possibly those sent to the Euston Associates investors) had ascribed the failures.

Jablon v. Dean Witter & Co., 614 F.2d 677 (9th Cir. 1980), and *Davis v. Birr, Wilson & Co.*, 839 F.2d 1369 (9th Cir. 1988), are distinguishable. They involved

sophisticated investors in public stocks with easy access to published market information obviously inconsistent with the representations. In contrast, in the case at bar, the software's poor performance was consistent with risks disclosed in the offering memoranda. As limited partners, appellants lacked easy access to further information as to their investments.

We cannot hold as a matter of law that appellants had inquiry notice of fraud as a result of the Lawrence Reports, offering memoranda, and Mt. Hood Associates "investment package." As discussed above, failure of the software did not necessarily suggest misrepresentations at offering time because the failure plausibly could have resulted instead from nonfraudulent realization of business risks disclosed by the offering memoranda and cited by the Lawrence Reports.

II

Imputed Knowledge

Under both Or. Rev. Stat. § 68.240 and Conn. Gen. Stat. § 34-50, notice to any partner "will operate as notice to, or knowledge of the partnership, except in the case of a fraud on the partnership committed by or with the consent of that partner.[2] We do not impute the knowledge of an agent to the principal where evidence shows that the former participated in the fraud. *See Admiralty Fund*, 677 F.2d 1310 (knowledge of president of plaintiff mutual fund could not be imputed to plaintiff because plaintiff alleged that president had participated in the fraud).

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[2]Because these provisions are the same, we need not resolve which state's law controls in order to reach our decision.

Questions of fact remain as to the extent of the general partners' knowledge which require resolution before the issues of whether such knowledge yielded inquiry notice and can be imputed to the limited partners arise. *Inter alia*, questions of fact exist as to the content of: (1) Burt's 1982 discussions with the Mt. Hood general partners regarding potential liability of defendants and possible misrepresentation of the software; and (2) Burt's disclosures to the Mt. Hood general partners regarding the results of Taylor's investigation into Poggel's charges.

III

Fraudulent Concealment

A plaintiff bears the burden of proving fraudulent concealment. *Conmar v. Mitsui & Co. (U.S.A.), Inc.*, 858 F.2d 499, 502 (9th Cir. 1988). As appellees contend, to toll the statutes of limitations under this theory, appellants most prove that: (1) appellees affirmatively concealed the existence of the causes of action; and (2) if appellants otherwise had inquiry notice, they diligently investigated the facts yielding notice but did not discover the existence of their claims because of the fraudulent concealment.

Because we hold that a question of fact arises as to whether appellants had inquiry notice, we need not consider whether appellants showed due diligence. *Id.* at 504-05. Also, a question of fact exists as to whether appellees affirmatively concealed appellants' claims by causing the general partners to hire Ward and installing Quenemoen as general partner or administrative assistant of all limited partnerships except LaMar (and by McKenna's denying to Taylor and Burt that any misrepresentation had occurred). Accordingly, factual

issues remain as to whether fraudulent concealment occurred that are not susceptible to summary judgment.

IV

RICO Claims

The Arnheim appellees argue for the first time on appeal that the district court correctly dismissed appellants' federal RICO claims because appellants failed to allege facts showing a pattern of racketeering activity as to these appellees. We do not decide this issue because it is appropriate for remand. *See Dandridge v. Williams*, 397 U.S. 471, 475-76 n.6 (1970) (quoting *United States v. American Railway Express Co.*, 265 U.S. 425, 435 (1924)), which states:

> "[T]he appellee may . . . urge in support of a decree any matter appearing in the record . . ." When attention [in the trial court] has been focused on other issues, or when the [lower] court . . . has expressed no views on a controlling question, it may be appropriate to remand the case rather than deal with the merits of that question [in the reviewing court] . . . .

V

Pendent Claims

Because the district court predicated dismissal of these claims on an incorrect view of the case, dismissal is vacated. The district court may revive these claims.

CONCLUSION

We emphasize that nothing we have said is intended to indicate any opinion regarding the resolution of the

factual issues on any of the questions involved in this case. We simply hold that genuine issues of material fact remain in each of these areas.

We REVERSE and REMAND for proceedings consistent with our holdings herein.

APPENDIX C

NOT FOR PUBLICATION

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

JOHN V. REITZ; JUDITH MACDONALD; DALE R. PETERSON; EARL D. RIDDLE; JACK E. EVANS; HARLAN C. SELBY; ROBERT E. JOHNSEN; PERRY COLEMAN; NICKOLAS J. MADESH; ROBERT A. GRAHAM; JERRY E. MARKS, et al.,
Plaintiffs-Appellants,

v.

LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.,; GLOBAL COMPUTER CORPORATION; RONALD JOHNSON; TEXCOM EQUIPMENT CORPORATION; COMDISCO, INC.; KENNETH M. PONTIKES; MARTIN KARNOFF; JOHN COSTELLO; DAVID MARKS; GORDON S. ROSEN ASSOCIATES, INC.; GORDON S. ROSEN; SOFTWARE SYSTEMS FOR WORD PROCESSORS, INC.; BERLENT INDUSTRIES, INC.; HARVEY BERLENT,
Defendants-Appellee.

No. 88-4077
D.C. Civ-86-1368-RE

ORDER

ANTHONY E. CATALAN,
Plaintiff-Appellant,

v.

PAULSON INVESTMENT COMPANY, INC.; LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW; COMPUTER VALUE ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; TECHNICAL MARKETING SERVICES, INC.; LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.,
Defendants-Appellees.

No.88-4099

D.C. CV-87-593-RE

JOHN GILBERTSON AND JANICE GILBERTSON, et al.,
Plaintiffs-Appellants,

v.

ANDERS G. ARNHEIM; ALANTHUS CORPORATION, formerly known as Technology Finance Group, Inc.; COMPUTER VALUE ASSOCIATES; AMERICAN COMPUTER EQUIPMENT LEASING; LEASING CONSULTANTS ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; WILLIAM MCKENNA; TEXCOM EQUIPMENT CORPORATION; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, et al.,
Defendants-Appellees.

No. 88-4100

D.C. CV-86-1369-RE

Before: PREGERSON, TROTT, and FERNANDEZ, Circuit Judges.

The panel has voted to deny the petition and to reject the suggestion for rehearing en banc.

The full court has been advised of the suggestion to rehear the case en banc, and no judge has requested a vote on it.

The petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED.

APPENDIX D

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

JOHN V. REITZ, et al.,
Plaintiffs,

v.

LEASING CONSULTANTS ASSOCIATES, et al.,
Defendants.

Civil No. 86-1368-RE

JOHN AND JANICE GILBERTSON, et al.,
Plaintiffs,

v.

LEASING CONSULTANTS ASSOCIATES, et al.,
Defendants.

Civil No. 86-1369-RE

ANTHONY E. CATALAN,
Plaintiff,

v.

PAULSON INVESTMENT COMPANY, INC., et al.,
Defendants.

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Pro Se Defendants.

REDDEN, Judge: These are three consolidated securities cases involving seven limited partnerships. Defendants move for summary judgment urging that the statutes of limitations bar plaintiffs' claims. I grant the motions.

BACKGROUND

I. Introduction

Plaintiffs seeking tax shelters invested in seven limited partnerships during the years 1979 through 1981. Tax problems arose, but plaintiffs did not then attempt to investigate their claims or file this action. When the tax shelters collapsed, plaintiffs paid no heed to their investments but instead sought to resolve their tax problems. Many plaintiffs became aware of the alleged securities claims only after attorneys for a potential defendant notified them of the possible claims in 1986. Plaintiffs, on the advice of counsel, waited several more months before filing. When plaintiffs settled with the Internal Revenue Service (IRS) they finally filed their complaints.

II. The Parties and the Structure of the Partnerships

These actions are identical for the purposes of these motions.

I noted in my June 17, 1987 Opinion that plaintiffs are limited partners in seven partnerships: Columbia Associates Limited Partnership (Columbia); Duval Associates Limited Partnership (Duval); Euston Associates Limited Partnership (Euston); Lamar Associates Limited Partnership (Lamar); Mt. Hood Associates Limited Partnership (Mt. Hood); Salem Associates Limited Partnership (Salem); and Troy Associates Limited Partnership (Troy). The actions involve several of the partnerships and sometimes different partners, and I refer to the plaintiffs by partnership.

Defendants are best identified by their various roles in the sales of partnerships and in operations of the partnerships themselves. The core defendants are those who organized and packaged the entire investment scheme.

The packagers are: Leasing Consultants Associates (LCA); Leasing Consultants, Inc. (LCI); William McKenna; Richard A. Heitmeyer; Richard D. Wellbrock; and William Ward.

In addition to the core defendants, several groups of additional defendants are involved. Each partnership involved purchases of certain IBM computer equipment (the hardware); and the purchase of various types of software equipment (the software). The scheme had an immediate seller purchase the equipment from the equipment seller, following which the partnership would purchase the equipment from the immediate seller. Then the partnership would lease the equipment back to the equipment seller or the affiliated lessee. In the hardware transactions, the hardware seller and lessee were the same but in the software transactions the software seller was affiliated with the software lessee. These two groups of sellers/lessees form another group of defendants. The immediate group of sellers are Computer Systems Consultants, Inc. (Computer Systems), LCI, LCA and American Computer Equipment Leasing, Inc. (American Computer).

The hardware equipment sellers/lessees are: Analysis International Co., Inc. (Analysis); Alanthus Computer Corp. (Alanthus); Comdisco, Inc. (Comdisco); and Rockwood Computer Corp. (Rockwood). The software equipment sellers are: Rosen Associates (Rosen); Kirby Microprocessors, Inc. (KMI); M.A. Hanson & Associates (Hanson); Robrech Systems, Inc. (Robrech); Buhler Software Services (Buhler); ASG Program Products, Inc. (ASG); and Start System, Inc. (Start). The affiliated software lessees are: Software Systems for Word Processors, Inc. (SSWPI) affiliated with Rosen; Kirby Computer Systems, Inc. (Kirby Computer) with KMI;

Prose, Inc. (Prose) with Hanson; Digitize, Inc. (Digitize) with Robrech; P-STAT, Inc. (P-Stat) with Buhler; Applications Systems Group, Inc. (Applications) with ASG; and Jeflen Consulting Corp. (Jeflen) with Start.

The remaining defendants are the equipment appraisers who evaluated the equipment and the attorneys who helped organize the partnerships and provided legal advice including a tax opinion. The hardware appraisers are Computer Value Associates (Value); Berlent Industries, Inc. (Berlent); TexCom Equipment Corp. (Texcom); and Global Computer Corp. (Global). The software appraisers are Technical Marketing Services, Inc. (TMS); Ward; Edward Fizell; ConServ International, Inc. (ConServ); and Information Industries, Inc. (Information). The attorneys are Lampf, Pleva, Lipkind, Prupis & Petigrow, P.C., and Arnheim & McCostis.

In addition to these, other defendants include affiliated entities and controlling persons of some of the abovementioned entities. I need not develop the roles of these defendants. A more detailed analysis of the parties and their roles is set forth in my June 17, 1987 Opinion.

Although the sales of the equipment were the same, the marketing of the equipment differed. Because the hardware was already in use at the time of the purchase, the hardware lessee did not have to find a sublessor for the equipment. The software, however, was novel. It had not been marketed and licensed prior to sale. The success of the software was key to the success of the limited partnerships. Each partnership targeted a different market and the software determined that market.

III. The Sale and Operation of the Partnerships

Plaintiffs purchased interests in the partnerships during the years 1979 through 1981. Plaintiffs allege that the packagers prepared investment memoranda for the partnership offerings and that they relied on these memoranda in making their investments. The memoranda contained statements involving the risk of investment, appraisals of the equipment and tax opinions.

General partners controlled each partnership. Roger Nelson and James Quenemoen controlled Duval and Troy; Richard Anderson controlled Lamar; Michael Welwood, Frank Leahy and Quenemoen controlled Mt. Hood; Robert Williams and Quenemoen controlled Columbia and Euston; J. Richard Hurst controlled Salem, and Nelson controlled Troy. Each partnership retained consultants. William Ward ultimately served as consultant for all.

Ward rendered his services through the Lawrence Group, Inc. Periodically, Ward provided the general partners with reports which discussed the status and problems of each partnership (the Lawrence Reports). According to defendants, the general partners sent these reports to the limited partners including plaintiffs.

IV. The Problems

The partnerships had trouble early on because of several factors, including technological obsolescence. Plaintiffs received reports that the software sales were dismal and the hardware's value was rapidly declining. With the possible exception of those in Lamar, plaintiffs received reports in late 1982 and early 1983 recommending a change in the character of the investments. In 1983,

Mt. Hood sold its software back to the seller and invested the proceeds in commercial real estate.

In late 1982 and early 1983, plaintiffs received notice that the IRS was investigating the partnerships. The law firm of Hagen & Dye represented most of the partnerships before the IRS.

Paulson Investment Co., which sold some of the partnership interests, sensed potential liability and retained the law firm of Stoll & Stoll. In mid-1986, the Stoll firm advised Paulson of significant liability exposure and suggested a way to eliminate that exposure. Paulson would fund plaintiffs lawsuit in exchange for plaintiffs' promises not to sue Paulson. In a "Dear Investor" letter, the Stoll firm advised plaintiffs it would file the lawsuit two months after the IRS's offer of settlement. The *Reitz* and *Gilbertson* plaintiffs accepted Paulson's offer and filed December 5, 1986.

Plaintiff Catalan declined Paulson's offer and filed an independent action in early June 1987, against Paulson and the defendants named in the other two cases. On January 5, 1988, Catalan agreed to dismiss Paulson with prejudice. Paulson, however, remains a third party defendant by virtue of a claim against it for indemnity and contribution. My Opinion of August 13, 1987 discusses this in greater detail.

V. The Allegations and the Record

The fourth amendment complaints (the complaints) allege that plaintiffs were induced to make the investments by several misrepresentations in the offering memoranda. Those misrepresentations are that the investments would entitle plaintiffs to substantial tax benefits; that the leasing of the hardware/software packages would

generate a profit; that the software was readily marketable; and that the equipment appraisals were reasonable and accurate. Plaintiffs allege that subsequent investigations revealed that these representations were false.

The complaints allege seven claims for the sales of the seven partnerships. Each claim contends the traditional several counts. Plaintiffs allege (1) violations of section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77(q)(a); (2) violations of section 10b of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b); (3) violations of Oregon securities laws, O.R.S. 59.135; (4) violations of federal RICO, 18 U.S.C. § 1962(c) and (d); (5) violations of the Oregon RICO statute, O.R.S. 165.720(3) and (4), O.R.S. 166.720(4); and (6) several common law claims for fraud, negligence and negligent misrepresentation against various defendants.

STANDARDS

Summary judgment is appropriate "if the pleadings, depositions, answers to interrogatories, and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact and that the moving party is entitled to a judgment as a matter of law." Fed. R. Civ. P. 56(c). The materiality of a fact is determined by the substantive law on the issue. *T.W. Electrical Service v. Pacific Electrical Contractors Ass'n,* 809 F.2d 626, 630 (9th Cir. 1987). The authenticity of a dispute is determined by whether the evidence is such that a reasonable party could return a verdict for the nonmoving party. *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 248 (1986).

The moving party has the burden of establishing the absence of a genuine issue of material fact. *Celotex Corp.*

v. Catrett, 477 U.S. 317, 323 (1986). If the moving party shows the absence of a genuine issue of material fact, then the nonmoving party must go beyond the pleadings and identify facts which show a genuine issue for trial. *Celotex*, 477 U.S. at 324.

Special rules of construction apply to evaluating summary judgment motions: (1) all reasonable doubts as to the existence of genuine issues of material fact should be resolved against the moving party; and (2) all inferences to be drawn from the underlying facts must be viewed in the light most favorable to the nonmoving party. *T.W. Electrical*, 809 F.2d at 630.

DISCUSSION

I. Introduction

Defendants move against the claim under section 17(a) and I grant the motion to dismiss. *In re Washington Public Power Supply System Securities Litigation*, 823 F.2d 1249, 1358 (9th Cir. 1987).

I later discuss defendants' motion against the pending state claims and grant it.

As to the statute of limitations issue, defendants argue that plaintiffs were on inquiry notice. Defendants say plaintiffs had direct knowledge of possible fraud with the receipt of the Lawrence Reports outlining the partnerships' dismal performance, and that plaintiffs knew of possible fraud by imputation, due to the knowledge of the general directors.

Plaintiffs challenge both of these contentions. As to the Lawrence Reports, plaintiffs argue that defendants have not shown their receipt of the reports, and further that even if they received same, the reports would not have put

a reasonable investor on notice. Plaintiffs also contend that even if they were on inquiry notice, defendants fraudulently concealed the relevant information from them. As to the knowledge by imputation, plaintiffs argue that the general partners exercised due diligence but failed to discover the fraud. Again, plaintiffs invoke the doctrine of fraudulent concealment.

II. The Statute of Limitations

A. Standards

The federal securities claims are subject to Oregon's two year statute of limitations for fraud, O.R.S. 12.110(1). *Robuck v. Dean Witter & Co.*, 649 F.2d 641, 643 (9th Cir. 1980). The limitations period for the federal RICO claims is four years. *Agency Holding Corp. v. Massey-Duff & Assoc., Inc.*, ____ U.S. ____, 107 S. Ct. 2759 (1987). There is a three year statute of limitations on the state securities claim, O.R.S. 59-115(b)(5) (1983) as well as on the common law claims, O.R.S. 12.110(1). A five year statute of limitations applies to the Oregon RICO claims, O.R.S. 166.725(11) (ORICO). If the statute of limitations bars the federal claims, including RICO, it will also bar all of the state claims except ORICO.

Federal law controls the point at which the statute of limitations commences to run for these federal claims. *Vold v. D.A. Davidson*, 816 F.2d 1406, 1412, 1415 (9th Cir. 1987). Normally, the period commences at the time of injury; for instance, in cases involving securities fraud, the investor suffers injury when he enters into a transaction as a result of a material misrepresentation. *Id.* at 1912. However, the statute of limitations is not triggered until the defrauded individual has actual or inquiry notice. That is, the statute begins to run when plaintiff in the exercise of due diligence discovered or should have dis-

covered the facts of which he complains. *Id. See Maggio v. Gerard Freezer & Ice Co.,* 824 F.2d 123, 129 (1st Cir. 1987) (noting that the statute commences when the investor should have known of the possibility of fraud).

As to inquiry notice, knowledge of all the facts is not necessary to commence the limitations period. *See Meadows v. Bicrodyne Corp.,* 785 F.2d 670, 672 (9th Cir. 1986). The clock begins to run when a plaintiff senses "storm warnings", *Cook v. Avien, Inc.,* 573 F.2d 685, 696 (1st Cir. 1978), not when he hears thunder and sees lighting. *Jensen v. Snelling,* 636 F. Supp. 1305, 1309 (E.D. La. 1986). A plaintiff is on inquiry notice if he possesses such knowledge as would alert a reasonable investor to the possibility of fraud. *Maggio,* 824 F.2d at 128.

B. Direct Knowledge: the Lawrence Reports

1. Individual Receipt of the Lawrence Reports

Plaintiffs would create a factual dispute regarding their receipt of the Lawrence Reports. They contend that defendants have failed to authenticate the reports or show the relevance of them. Plaintiffs, however, produced the reports and concede receipt by alleging that these reports lulled them into inaction. Defendants have shown that the Lawrence Reports were sent with the periodic reports from the general partners. There is no genuine issue of material fact as to plaintiffs' receipt of the Lawrence Reports.

2. The Contents of the Reports

The Lawrence Reports showed that although the investment memoranda projected significant sales, the partnerships showed no sales. These dismal reports continued until 1982, when Ward recommended considering other options. Most of the partnerships considered return of the software during 1982, but only Mt. Hood opted for return and reinvestment in real estate.

The Mt. Hood plaintiffs whose partnership closed on September 29, 1980, received a June 29, 1981 report indicating no software sales; a November 14, 1981 report indicating that of 140 projected sales, none had been made, and the marketing effort was very poor. They also received a May 17, 1982 report stating that the software marketing was unsuccessful and urging other options, as well as a June 6, 1983 report indicating that the value of the hardware was declining sharply.

The Salem partnership experienced similar difficulties. As early as December 1981, the software required re-programming to run on different hardware. During the same period, the sales of the software licenses were at a standstill, and by July 1982, the required re-programming was not yet complete. It was reported that re-programming was not worthwhile, and that there were no current sales.

The Lamar partnership suffered a similar plight. In his appraisal, Ward indicated that eight hundred software licenses would be sold in the first three years. Anderson, the general partner, indicated in 1981 that only one license had sold. Anderson also reported that the software needed revision which could cost as much as $50,000. He also reported new loans to Robrech and

Digitize. Finally in October 1982, Anderson reported that only three licenses had been sold.

The remaining partnerships experienced similar difficulties. The reports of the general partners, as well as the Lawrence Reports indicated that the software licenses were not selling and the software required re-programming. These problems with the all-important software sales should have given notice to a reasonable investor that something was amiss.

In addition to these reports, plaintiffs also received reports that the hardware was declining sharply in value. Plaintiffs also received information that the rental income from the hardware had been deferred or was unpaid.

3. Conclusion

I find that the Lawrence Reports would have placed a reasonable investor on notice of the possibility of fraud as early as the fall of 1982. Plaintiffs contend that they exercised due diligence by relying on the reports of the general partners and on the Lawrence Reports. Plaintiffs argue that these reports were consistent with the offering memoranda and contained no specifics as to the facts underlying their claims. They also contend that defendants fraudulently concealed the true scope of the problems through these reports. These arguments are not supported by the record or the law.

If the contents of the reports were consistent with the offering memoranda, then the offering memoranda put plaintiffs on sufficient notice of the possibility of fraud. The reports need not contain the details of the fraud to trigger inquiry notice but need only put plaintiffs on notice of the possibility of fraud, e.g., their investment was worth less at investment time than they actually paid for it.

I find that the Lawrence Reports put plaintiffs on inquiry notice of the possibility of fraud. The reports did not conceal their claims.

C. Notice by Imputation

1. Introduction

In addition to the Lawrence Reports, the general partners had access to other sources of information such as reports from their attorneys and the allegations of an offeree representative, George Poggel. Defendants argue that such knowledge constituted notice of the possibility of fraud and should be imputed to plaintiffs.

The limited partnerships were Connecticut corporations and the interests were sold in Oregon. Both Oregon and Connecticut recognize that notice to or knowledge of the general partners regarding matters relating to the partnership operate as notice to or knowledge of the partnership. O.R.S. 68.240; Conn. Gen. Stat. §§ 34-50. Both states also recognize that fraud on the partnership committed by or with consent of the partner bars imputation. O.R.S. 68.240; Conn. Gen. Stat. §§ 34-50. There is no conflict of laws problem, and I apply the law of the forum, Oregon. *See Klaxon v. Stentor Electric Manufacturing Co.*, 313 U.S. 487 (1941).

Defendants point out that the general partners knew of the problems in early 1982, and focus their discussions on Quenemoen who was a general partner of or connected to all of the partnerships save Lamar. Plaintiffs do not suggest that Anderson, Lamar's general partner, had no such notice. Anderson advised the limited partners of the poor sales as early as 1981, and of the IRS audit in October 1982. Defendants also point out that several other events put the general partners on notice of the possibility of fraud.

Plaintiffs argue that the general partners exercised due diligence and discovered no fraud. They also argue that the general partners were part of or consented to the fraud.

2. The General Partner's Knowledge

a. The Burt Report

In July 1982, Mt. Hood retained attorney Robert Burt to represent them in the IRS investigation. Burt's investigation led him to believe that defendant LCI might be liable by reason of misrepresentation, fraud, negligence and breach of contract. Although defendants indicate that most of Burt's discussions were with Welwood, Burt indicated that all of Mt. Hood's general partners, including Quenemoen, decided not to pursue these claims for business reasons. Defendants argue that Quenemoen's knowledge acquired in the Mt. Hood investigation should be imputed to the other partnerships in which he participated.

b. The Poggel Allegations

To effect the Mt. Hood change in investments, Burt prepared an extensive information packet which explained the exchange. George Poggel, the offeree representative for plaintiff Marchette, responded to the packet alleging possible fraud, conflicts of interest and possible criminal violations. Burt had an associate, Dana Taylor, investigate the allegations. According to Taylor his investigation was limited to a possible conflict of interest. The result of the Taylor investigation were negotiations in 1982 over a proposed indemnity agreement between defendants LCI, LCA, Hamilton Resources and McKenna, and the Mt. Hood partnership. Ultimately, the parties reached a narrower agreement. However, defendants contend that the fact that the general partners attempted to

secure such an agreement indicates that they feared securities claims.

3. Conclusion

I find that both sources, as well as the Lawrence Reports, put the general partners on inquiry notice of the possibility of fraud. Indeed, Burt suggested this possibility. Further, the very reports of the general partners indicated that the investments had significant problems and might not be worth as much as plaintiffs paid for them.

Plaintiffs contend that the general partners exercised due diligence and did not discover the facts underlying their claims. As to the Burt report, plaintiffs contend that he never performed any factual investigation to determine or substantiate the possible liability. However, as noted above, Burt suspected the possibility of fraud, and this knowledge is sufficient for inquiry notice.

Further, as to the Poggel allegations, plaintiffs contend that Taylor's investigation satisfied the due diligence requirement. According to plaintiffs, Poggel only complained of a possible conflict of interest and Taylor's investigation was limited to this issue. However, as noted above, the Poggel allegations went beyond a conflict problem and also raised the possibility of fraud.

III. Fraudulent Concealment

A defendant's conduct may serve to toll the statute of limitations if it is established that the defendant intentionally concealed the fraud. *Volk,* 816 F.2d at 1415, 1416. To establish fraudulent concealment, plaintiff must demonstrate affirmative conduct on the defendant's part which, under the circumstances, would lead a reasonable person to believe that he did not have a claim. *Id.*

Plaintiffs contend that defendants fraudulently concealed the securities problems in two ways: (1) the Lawrence Reports lulled plaintiffs into inaction; and (2) LCI installed Quenemoen as general partner. Plaintiffs contend that the Lawrence Reports were consistent with the risks disclosed in the various offering memoranda, and point out that the reports were not entirely negative.

However, this argument cuts two ways. If the investment memoranda disclosed the risks, then plaintiffs were on notice at the time of purchase. If investment memoranda contain conflicting data on the investment, plaintiffs cannot choose the positive without taking into account, i.e., being on notice, of the negative. *Kennedy v. Josephthal & Co., Inc.*, 814 F.2d 798 (1st Cir. 1987).

Further, as noted above, I find that the Lawrence Reports put plaintiffs on inquiry notice. If these reports and those of the general partners put plaintiffs on inquiry notice, then the same reports could not have concealed the fraud.

Plaintiffs say Quenemoen was a former LCI employee and that he was installed as general partner by LCI. They offer nothing to suggest that the prior association was improper or that Quenemoen was actively engaged in the fraud or consented to it. Even if Quenemoen consented to the fraud, his knowledge may be imputed for the sake of third parties not participating in the fraud. *Armstrong v. Ashley*, 204 U.S. 272 (1907).

IV. Conclusion

I find that plaintiffs were on inquiry notice, either directly or indirectly, of the possibility of fraud as early as October 1982. The *Reitz* and *Gilbertson* plaintiffs filed in December 1986. Catalan filed in June 1987. Therefore, all the federal claims are barred by the relevant statutes of limitations.

Only the ORICO claim remains. I decline to exercise pendent jurisdiction over this state claim, and I dismiss it for want of subject matter jurisdiction.

I grant defendants' motions for summary judgment.

Dated this 13th day of July, 1988.

JAMES A. REDDEN

James A. Redden
United States District Judge

Supreme Court, U.S.
FILED
SEP 14 1990
JOSEPH F. SPANIOL, JR.
CLERK

(3)

No. 90-333

In The

Supreme Court of the United States

October Term, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,

Petitioner,

vs.

JOHN GILBERTSON, JOHN V. REITZ, and ANTHONY CATALAN, et al.,

Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONSE TO BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

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QUESTIONS PRESENTED

1. Is there a conflict among the circuits on the statute of limitations for 10b-5 actions?

2. Does the lack of a uniform statute of limitations for 10b-5 actions result in chaos and confusion?

3. Would a federal statute of limitations for 10b-5 actions barring any claims more than three years after the violation, regardless of when the injured party discovered the violation, further the policy and objectives of a private right of action under Rule 10b-5?

4. Should an outright change in the statute of limitations, which has not been "foreshadowed," be applied retroactively to bar claims which were viable under the existing statute of limitations at the time the suit was filed?

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On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

RESPONSE TO BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

STATEMENT OF THE CASE

Factual Background

Respondents accept petitioners' Statement of the Case with the following corrections. Petitioners did not "allegedly assist" in preparing the offering memorandum, they prepared it totally. Petitioners prepared all the closing documents, the offering memorandum, and the tax opinion. Petitioners prepared instructions for the

salesmen. Petitioners received investors' funds and made disbursements.

The limited partnership were *very* fraudulent. In several, the assets which were supposed to be purchased at closing with the investors' money were not purchased at all. Fraudulent paperwork was prepared to show nonexistent purchases. The funds were stolen. Each partnership purchased a software tape purportedly worth about $2,000,000. None of the seven software tapes ever generated more than trace amounts of revenue. The appraisals supplied to investors were lies.

The general partners were friends and close business associates of the promoters. If they became aware of facts suggesting the fraudulent nature of the partnerships, they certainly did not communicate them to the respondents, limited partners. They did the opposite. They permitted the promoters to send the investors a series of "expert reports" explaining the partnership problems and lack of profitability. The explanations appeared reasonable, and never, of course, suggested fraud.

When the IRS challenged the valuations of the partnership assets, the general partners were forced to hire outside counsel. The lawyers discovered the fraud while investigating the value of the assets. Because of the involvement of outside counsel and the imminence of IRS problems, the facts suggesting fraud were finally communicated to the respondents.

Suit was filed within a year after plaintiffs learned of those facts.

Proceedings Below

Respondents accept petitioner's summary of the proceedings in the district and circuit courts.

REASONS FOR DENYING THE WRIT

I.

THERE HAS ALWAYS BEEN CONFLICT WITHIN AND AMONG THE CIRCUITS ABOUT THE STATUTE OF LIMITATIONS FOR 10b-5 ACTIONS; THE THIRD CIRCUIT DECISION IN *IN RE DATA ACCESS SYSTEMS SECURITIES LITIGATION*, 843 F.2d 1537 (3d Cir.) (en banc), cert. denied, ___ U.S. ___, 109 S.Ct. 131, 102 L.Ed.2d 103 (1988), HAS NOT INCREASED THE CONFLICT.

Before *In Re Data Access, supra*, all federal courts looked to state law for the applicable statute of limitations. There were fifty different rules creating differences within and between circuits. *In Re Data Access* standardizes the rule within the Third Circuit. To that extent, *In Re Data Access* has reduced conflict, not increased it.

The Third Circuit read this Court's decisions in *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), and *Del Costello v. Teamsters*, 462 U.S. 151 (1983), as permission to look to federal law for the statute of limitations in 10b-5 cases. Those cases did invite federal courts to consider federal law in determining the most analogous statute of limitations for federal causes of action. Nothing in those cases suggested a preference for federal law unless federal law is more analogous than state law. There are just more analogies to consider.

The fact that one circuit has chosen a federal law as the appropriate analogy in 10b-5 cases does not create a conflict between the circuits. It simply reflects the fact that this Court's decisions in *Agency Holding Corp.* and *Malley-Duff* make more choices available.

II.

THE PRESENT SITUATION IS NOT "CHAOTIC". Brief for Petitioner, p. 8.

For reasons stated above, the situation after *In Re Data Access, supra,* is, if anything, less complicated than it was before the decision. There are decisions in each federal district deciding which state statute of limitations applies to 10b-5 actions. Litigants bringing 10b-5 actions are not confused about the applicable statute of limitations. We doubt that any judicial time or energy is spent deciding which statute of limitations applies.

There is undoubtedly forum shopping where a 10b-5 action may be brought in more than one state and the statutes of limitations differ. The fact of forum shopping is not an imposition on the federal court system, and it does not require this Court's attention. If the case is brought in a proper forum, it is unimportant that the statute of limitations was a consideration.

A national statute of limitations for 10b-5 actions would be conceptually tidy and, for that reason, desirable. As will be discussed next, petitioner's proposal for conceptual tidiness would be purchased at the price of greatly reducing the effectiveness of 10b-5 to deter and remedy securities fraud.

III.

A STATUTE OF LIMITATIONS FOR SECURITIES FRAUD WHICH CANNOT BE TOLLED FOR CONCEALMENT IS UNFAIR AND ONLY PARTIALLY EFFECTIVE.

In *In Re Data Access*, 843 F.2d 1537, 1550 (3d Cir. 1988), the Third Circuit imposed a three year statute of limitations regardless of defendant's efforts at concealment and plaintiff's inability to discover the fraud:

> Accordingly, we have decided that the proper period of limitations for a complaint charging violation of section 10(b) and Rule 10b-5 is one year after the plaintiff discovers the facts constituting the violation, and in no event more than three years after such violation.

843 F.2d 1550. The last clause appears to say that the defendant who has committed fraud wins if he or she successfully conceals the fraud for three years, or if the plaintiff, with or without fault on his or her part, remains ignorant of the fraud for three years.

As the present case demonstrates, where promoters commit securities fraud, they do not intend to be immediately sued or indicted. They intend to enjoy their ill-gotten gain. Fraud is by nature concealment of the truth by misrepresentation or omission. A statute of limitations which cannot be tolled for successful concealment, and which, in effect, rewards successful concealment, is not a desirable statute of limitations for a fraud action.

This Court has frequently recognized that a fraud statute of limitations must be tolled where the fraud has been concealed or where the plaintiff has failed to discover the fraud through no fault of his or her own. *Bailey*

v. Glover, 88 U.S. 342 (1875); *Exploration Co. v. United States*, 247 U.S. 435 (1917); *Holmberg v. Armbrecht*, 327 U.S. 392 (1945); and *American Pipe and Construction Co. v. Utah*, 414 U.S. 538 (1974).

Bailey, supra, was a fraud action in equity subject to a statute of limitations in the "Bankrupt Act" stating that "no suit in law or in equity shall in any case be maintained . . . unless brought within two years. . . . " 88 U.S. at 348-349. The Court held that the equitable rule that "the bar of the statute does not begin to run until the fraud is discovered" also applies to statutes of limitations in cases at law.

> We also think that in suits in equity the decided weight of authority is in favor of the proposition that where the party injured by the fraud remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party.
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> * * *
>
> But we are of opinion, as already stated, that the weight of judicial authority, both in this country and in England, is in favor of the application of the rule to suits at law as well as in equity. And we are also of opinion that this is founded in a sound and philosophical view of the principles of the statutes of limitation. They were enacted to prevent frauds; to prevent parties from asserting rights after the lapse of time had destroyed or impaired the evidence which would show that such rights never existed, or had been satisfied, transferred, or extinguished, if they ever did exist. To hold that by concealing

> a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure. And we see no reason why this principle should not be as applicable to suits tried on the common-law side of the court's calendar as to those on the equity side.

88 U.S. at 348-349.

In *Exploration Co., supra*, the defendant "talked very freely" about the fraud by which he had obtained and concealed an illegal land patent after the six year statute of limitations on suits to vacate patents had expired. 247 U.S. at 445-446. The government sued, asserting the rule in *Bailey, supra*. This Court reaffirmed *Bailey*, holding that the statute of limitations had been tolled, even though it made no provision for tolling.

> When Congress passed the act in question the rule of *Bailey v. Glover* was the established doctrine of this court. It was presumably enacted with the ruling of that case in mind. We cannot believe that Congress intended to give immunity to those who for the period named in the statute might be able to conceal their fraudulent action from the knowledge of the agents of the Government. We are aware of no good reason why the rule, now almost universal, that statutes of limitations upon suits to set aside fraudulent transactions shall not begin to run until the discovery of the fraud, should not apply in favor of the Government as well as a private individual. It is not our belief that Congress intended that the Government should be deprived of title to public lands by those who added to the fraud by which they were

> obtained, artifices which enabled them to conceal the fraudulent manner in which they were secured until the action was supposed to be barred by the lapse of six years.

247 U.S. at 449-450.

The rule in *Bailey* was again reaffirmed in *Holmberg, supra.*

> And so this Court long ago adopted as its own the old chancery rule that where a plaintiff has been injured by fraud and "remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party." *Bailey v. Glover*, 21 Wall. 342, 348; and *see Exploration Co. v. United States*, 247 U.S. 435; *Sherwood v. Sutton*, 5 Mason 143.
>
> This equitable doctrine is read into every federal statute of limitation.

327 U.S. at 397.

In *American Pipe and Construction Co., supra*, this Court held that public bodies and state agencies in Utah, purported class members in an unsuccessful antitrust class action for damages, could intervene in a similar antitrust action for damages brought by the State of Utah, after the statute of limitations had expired. The class action was timely filed, but class status was denied after the statute had expired. The potential class members then intervened individually in the action brought by the State. In so holding, this Court reaffirmed *Holmberg*, emphasizing that the power of the federal courts to toll a

federal statute of limitations is "deeply rooted in our jurisprudence."

> Similarly, in cases where the plaintiff has refrained from commencing suit during the period of limitation because of inducement by the defendant, *Glus v. Brooklyn Eastern Terminal*, 359 U.S. 231, or because of fraudulent concealment, *Holmberg v. Armbrecht*, 327 U.S. 392, this Court has not hesitated to find the statutory period tolled or suspended by the conduct of the defendant. In *Glus, supra*, the Court specifically rejected a contention by the defendant that when 'the time limitation is an integral part of a new cause of action . . . that cause is irretrievably lost at the end of the statutory period.' 359 U.S., at 232. To the contrary, the Court found that the strict command of the limitation period provided in the federal statute was to be suspended by considerations '[d]eeply rooted in our jurisprudence.' Ibid.
>
> These cases fully support the conclusion that the mere fact that a federal statute providing for substantive liability also sets a time limitation upon the institution of suit does not restrict the power of the federal courts to hold that the statute of limitations is tolled under certain circumstances not inconsistent with the legislative purpose.

414 U.S. at 559.

Despite this Court's repeated insistence on interpreting all federal statutes of limitations in fraud cases to permit tolling where the plaintiff is unaware of the fraud through no fault of his or her own, the petitioner is asking this Court to impose on all 10b-5 actions a statute of limitations which, by its terms, appears to preclude any such flexibility. The result would be to reduce the

scope of 10b-5, to reward perpetrators of securities fraud who are able to conceal it, and to deny the remedy to defrauded investors who are unaware of the fraud through no fault of their own.

IV

THE STATUTE OF LIMITATIONS SHOULD NOT BE RETROACTIVELY SHORTENED TO BAR RESPONDENTS' FRAUD CLAIMS.

If this Court issues a writ of certiorari, whether the statute of limitations should be changed retroactively to bar respondents' fraud claims will be a major issue.

CONCLUSION

This Court denied certiorari when *In Re Data Access* was decided. The rule in that case offers simplicity where it is not needed. The statute of limitations for 10b-5 actions is very clear in every state. The simplicity offered by uniform application of the *In Re Data Access* rule would be purchased at the cost of this Court's historic insistence that statutes of limitations for fraud be tolled for investors who, through no fault of their own, have not discovered the fraud.

This Court's decisions in *Malley-Duff* and *Del Costello* have given the lower courts new options for finding the appropriate statute of limitations for federal causes of action. The Third Circuit rule in *In Re Data Access*, recently rejected by the Ninth and Eleventh Circuits, demonstrates that the lower courts are just starting to

consider whether a uniform rule in 10b-5 cases is necessary, and, if so, what it should be. *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990); *Smith v. Duff and Phelps, Inc.*, 891 F.2d 1567, 1569-70 (11th Cir. 1990).

The choices presented by this case are not good ones: reaffirming the multiplicity of state statutes or adopting a uniform federal statute of limitations which prohibits tolling. If a uniform federal statute of limitations is a good idea, the lower courts will eventually present this Court with better alternatives.

Respectfully submitted,

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No. 90-333

In the Supreme Court

OF THE

United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,
Petitioner,

VS.

JOHN GILBERTSON, JOHN V. REITZ, and
ANTHONY CATALAN, *et al.*,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

SUPPLEMENTAL BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

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SUPPLEMENTAL BRIEF FOR PETITIONER LAMPF PLEVA LIPKIND PRUPIS & PETIGROW

Pursuant to Supreme Court Rule 15.7, Petitioner Lampf, Pleva, Lipkind, Prupis & Petigrow submits this Supplemental Brief in support of its Petition for a Writ of Certiorari.

I.

THE SEVENTH CIRCUIT HAS RECENTLY HELD FEDERAL LAW PROVIDES THE LIMITATIONS PERIOD FOR CLAIMS UNDER SECTION 10(b) OF THE SECURITIES EXCHANGE ACT OF 1934, FURTHER WIDENING THE GROWING SPLIT AMONG AND WITHIN THE CIRCUITS

Petitioner Lampf, Pleva, Lipkind, Prupis & Petigrow has filed a Petition for a Writ of Certiorari for the purpose of having this Court answer the question of whether state or federal law provides the limitations period for actions under section 10(b) of the Securities Act of 1934 (15 U.S.C. § 78*j*(b)) and Rule 10b-5 (17 C.F.R. 240.10b-5) promulgated thereunder. Lampf's brief in support of its petition discusses the reasons why this Court should grant the petition, including the split that exists among and within the circuits on this issue. The conflict among the circuits has recently increased as the Seventh Circuit Court of Appeals has joined the growing number of courts that have held that federal law, rather than state law, should provide the limitations period for section 10(b) claims.

In *Short v. Belleville Shoe Manufacturing Co.*, 908 F.2d 1385 (7th Cir. 1990), the court held that federal and state law supplies the statute of limitations in suits under section 10(b) and Rule 10b-5.[1] The Seventh Circuit thus joins the Third Circuit in holding that section 10(b) claims are governed by a uniform federal statute of limitations. *See In Re Data Access Securities Litigation*, 843 F.2d 1537 (3d Cir.) (en banc), *cert. denied*, ____ U.S. ____, 109 S.Ct. 131, 102 L.Ed.2d 103 (1988).

---

[1]The *Short* decision is reprinted at Appendix A to this Supplemental Brief.

The plaintiff in *Short* filed suit under section 10(b) twelve years after defendant redeemed 550 shares of its stock from plaintiff. Plaintiff alleged that at the time it redeemed plaintiff's stock, the defendant corporation fraudulently painted a gloomy picture of its future prospects. The district court dismissed plaintiff's claims on the grounds the plaintiff had failed to commence her action within the time allowed by law. On appeal, defendant urged the Seventh Circuit to abandon its practice of looking to state law for the applicable statute of limitations and instead apply a limitations period derived from federal law.

The Seventh Circuit began its analysis by acknowledging that for at least 18 years it had looked to state law for the statute of limitations for section 10(b) claims. (A-2.) However, the court admitted it had applied state laws as a matter of habit and without analyzing whether it was more appropriate to look to federal law for the limitations period. (A-3.)

The court then evaluated the competing justifications for applying either state or federal law, and found that federal law was the superior choice.

The court first noted that it was fanciful to presume — as some court do — that by its silence regarding the statute of limitations, Congress intended for the courts to look to state law for the statute of limitations. The Seventh Circuit found this reasoning unpersuasive because the *courts* created the cause of action under Section 10(b). Consequently, there is no reason to infer that *Congress* had any intent whatsoever. (A-3-4.)

The court next noted that in fact Congress had not been silent regarding limitations periods, but instead had provided an express limitations period for each express

statutory right of action in the securities laws. (A-4.) Accordingly, the court said "[t]here can be no presumption that Congress meant courts to look to state law, when every time Congress has authorized a federal remedy it has also created a federal period of limitations." (A-4.)

The court recognized that application of state law to multi-state transactions was inconsistent with the spirit of the federal securities laws. Congress enacted the federal securities laws "because it believed that national law ought to govern multi-state transactions. Returning to state law to fetch a period of limitations is inconsistent in spirit with this decision." (A-4.)

The Seventh Circuit then considered whether the Rules of Decision Act, 28 U.S.C. § 1652 *requires* courts to look to state law for the limitations period. The court found no such requirement, drawing guidance from this Court's decisions in *Del Costello v. Teamsters*, 462 U.S. 151 (1983) and *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), where this Court held that federal and not state law provided the most appropriate limitations period for federal causes of action. (A-5.)

Finally, the court examined whether selection of a federal statute of limitations was consistent with this Court's statement that a federal limitations period should be selected "when a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking," *Del Costello*, 462 U.S. at 171-72, quoted in *Agency Holding*, 483 U.S. at 148. In *Short*, the Seventh Circuit held that securities law satisfies this Court's standard.

The court first held that federal law "clearly provides a closer analogy than available state statutes" because the federal securities laws contain express actions and limitations periods for the very type of conduct regulated by section 10(b) — misrepresentations and omissions in connection with the sale of securities. (A-5.) For example, section 12 of the Securities Act of 1933 (15 U.S.C. § 77*l*) concerns incorrect statements and material omissions in the sale of securities. Section 12 is subject to an express limitations period contained in section 13 of the 1933 Act (15 U.S.C. § 77*m*). State law could provide no more analogous statute.

The court further held that the "practicalities of litigation" compelled the selection of a uniform federal limitations period because "[f]rom the perspective of practitioners litigating cases originating in many states (especially class actions), the situation is a nightmare." (A-7.) The court bemoaned (1) the "untold hours" wasted by lawyers and courts identifying the proper state statute of limitations, (2) the unfairness resulting from the unjustified disparities in the rights of parties litigating identical claims in different states, (3) the promotion of forum shopping by plaintiffs, and (4) the utter lack of certainty and predictability for parties working in the securities field. (A-7.)

After considering these several issues, the court held that "federal and not state law supplies the statute of limitations in suits under §10(b) and Rule 10b-5." (A-8.) By so holding, the court widened the split among the circuits on this important issue of federal law. The Seventh Circuit's decision emphasizes the need for this Court

to grant the petition for the purpose of resolving this issue.

Respectfully submitted,

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IN THE
United States Court of Appeals
FOR THE SEVENTH CIRCUIT

No. 89-3271

MARIAN W. SHORT,
Plaintiff-Appellant,

vs.

BELLEVILLE SHOE MANUFACTURING COMPANY, *et al.*,
Defendants-Appellees.

Appeal from the United States District Court
for the Southern District of Illinois, Alton Division.
No. 89-5061 — William L. Beatty, *Judge.*

Argued June 12, 1990 — Decided July 30, 1990

Before POSNER, EASTERBROOK, and MANION, *Circuit Judges.*

EASTERBROOK, *Circuit Judge.* Belleville Shoe Manufacturing Company redeemed 550 shares of its stock from Marian Short in 1977, paying $273 per share. Twelve years later Short filed this suit under § 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and the SEC's Rule 10b-5, 17 C.F.R. § 240.10b-5, contending that Belleville (a closely-held, family corporation) and its controlling shareholders had defrauded her about the value of the shares. They painted a gloomy picture of the firm's prospects in 1977; it has prospered since. Short depicts her brother Homer Weidmann, an officer of Belleville, as her principal business adviser and contends that she delayed filing suit because Weidmann repeatedly assured her that she had received a fair price in 1977.

The district court dismised the case under Fed. R. Civ. P. 12(b)(6), concluding that Short could not escape the statute of limitations. Short relies on state and federal tolling rules. Defendants respond that we should not inquire into tolling because § 13 of the '33 Act, 14 U.S.C. § 77m, which they ask us to apply, sets three years as an unyielding limit. Defendants ask, in other words, that we cease looking to state law as a source of periods of limitations in securities cases, on the authority of *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), which applied a federal statute of limitations (from the antitrust laws) to cases under the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. §§ 1961-68.

I

A

For many years we have applied to cases under Rule 10b-5 statutes of limitations borrowed from state blue sky statutes, adding an overlay of tolling principles from state and federal law. *Davenport v. A.C. Davenport & Son Co.*, 903 F.2d 1139 (7th Cir. 1990), is the most recent in a line going back at least to *Parrent v Midwest Rug Mills, Inc.*, 455 F.2d 123, 125-27 (7th Cir. 1972). See also, e.g., *Norris v. Wirtz*, 818 F.2d 1329 (7th Cir. 1987); *Teamsters Local 282 Pension Trust Fund v. Angelos*, 815 F.2d 452 (7th Cir. 1987); *Suslick v. Rothschild Securities Corp.*, 741 F.2d 1000 (7th Cir. 1984); *Goldstandt v. Bear, Stearns & Co.*, 522 F.2d 1265 (7th Cir. 1975); *Tomera v. Galt*, 511 F.2d 504 (7th Cir. 1975). Like the other courts of appeals, we looked to state law because Congress has not enacted a statute of limitations for Rule 10b-5, and could hardly have been — for the right of action under Rule 10b-5 was created by the courts rather than Congress. Section 10(b)

itself grants rulemaking authority to the SEC; because it does not create a right of action, it is not accompanied by a statute of limitations.

Because Congress was silent, we applied the principle, derived from the Rules of Decision Act, 28 U.S.C. § 1652, that when federal law is deficient, state law fills the gap. One of the venerable applications is to obtain periods of limitations from state law. E.g., *Auto Workers v. Hoosier Cardinal Corp.*, 383 U.S. 696, 704 (1966) (collecting cases). This is so predictable that Congress may anticipate it, so that when it does not enact a federal statute of limitations it means to leave in place the background rule that state law applies. See *Reed, v. United Transportation Union*, 109 S. Ct. 621, 625 (1989); *Agency Holding*, 483 U.S. at 147; *DelCostello v. Teamsters*, 462 U.S. 151, 158 (1983). Federal courts are so accustomed to turning to state periods of limitations that we (and our colleagues in other circuits) did this on auto-pilot, without discussing whether something differentiated securities laws from other statutes. See also *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 2120 n.29 (1976); *Herman & Mac Lean v. Huddleston*, 459 U.S. 375, 384 n.18 (1983), both recognizing the prevailing practice.

Yet there are differences. One is that Congress could hardly have anticipated that courts would turn to state law for a period of limitations, when Congress did not create the right to action in the first place. We are not dealing here with a problem of deciding whether Congress meant to *depart* from a norm; we have a problem of the courts' creation. See *United Parcel Service, Inc. v. Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring); *DelCostello*, 462 U.S. at 158-59 n.12. Federal courts have an obligation to create stable periods of limitations for

their handiwork. *Smith v. Chicago,* 769 F.2d 408 (7th Cir. 1985).

A second difference is that Congress has not been silent. The securities acts are jammed with statutes of limitations. For every statutory right of action there is a corresponding statute of limitations. The Securities Act of 1933 gave the purchaser two years from the date of discovering the fraud, but in no event more than ten years from the date of sale. 48 Stat. 84 (1933). When Congress enacted the '34 Act, it amended this statute (now § 13 of the '33 Act) and added four more, one for each of the new express rights of action. See §§ 9(e), 16(b), 18(c), and 29(b), 15 U.S.C. §§ 78i(e), 78p(b), 78r(c), and 78cc(b). In 1988 it added another for inside trading cases, 102 Stat. 4680-81, to be codified as §20A, 15 U.S.C. § 78t-1. There can be no presumption that Congress meant courts to look to state law, when every time Congress has authorized a federal remedy it has also created a federal period of limitations.

Third, turning to state law for periods of limitations creates special problems under the securities acts because the acts do not apply in the first place unless the transactions occurred in interstate commerce. At least two state statutes therefore could be applied to any case. Courts must use conflict-of-laws principles to pare the number down to one. Congress enacted a national rule against fraud because it believed that national law ought to govern multi-state transactions. Returning to state law to fetch a period of limitations is inconsistent in spirit with this decision.

All of this would be by the by if the Rules of Decision Act *requires* federal courts to use state law. But two cases decided after the courts of appeals began to apply state law under Rule 10b-5 hold that it does not. *DelCostello*

concluded that a six-month period drawn from the National Labor Relations Act governs "hybrid" suits alleging an employer's breach of contract coupled with a union's breach of the duty of fair representation. *Agency Holding* decided to apply the four-year period of limitations in the antitrust laws to suits under RICO. These cases call for fresh examination of the question whether to turn to state law in securities cases. The third circuit conducted such an examination and concluded that § 13 of the '33 Act is the appropriate statute. *In re Data Access Systems Securities Litigation,* 843 F.2d 1537 (3d Cir. 1988) (in banc). The Securities and Exchange Commission likewise believes that federal law supplies the period of limitations, although it thinks that the new § 20A rather than §13 is the closer match. Brief for the United States as Amicus Curiae in *Lebman v. Aktiebolaget Electrolux,* No. 88-1144 (October Term, 1988), *cert. denied,* 109 S. Ct. 3214 (1989). The time is ripe for reconsideration in this circuit too.

"[W]hen a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking", *DelCostello,* 462 U.S. at 171-72, quoted in *Agency Holding,* 483 U.S. at 148, it is appropriate to select a federal statute of limitations. Securities law satisfies both branches. The statutes of limitations in the securities acts are addressed to the conduct at stake in this case — securities fraud. Section 13, in particular, covers the express right of action in § 12, which concerns incorrect statements and material omissions in the course of selling securities. Congress has spoken directly to the appropriate statute of limitations for litigation of the sort Short presses. When the statute contains not only a statute of limitations for

every express right of action, but also an express right of action quite similar to the implied right of action, then the federal statute "clearly provides a closer analogy than available state statutes".

Difficulties in selecting an appropriate state statute also influence the "practicalities of litigation". Even when turning to state law, courts should endeavor to find a single period of limitations "that can be applied with ease and predictability in all 50 States." *Owens v. Okure,* 109 S. Ct. 573, 578 (1989). That task has proved daunting in securities cases. Different courts have looked to different bodies of state law for inspiration. Some borrow from the statute generally applicable to fraud; some borrow from state blue sky laws; some courts use a little of each, depending on the particulars of the claim under Rule 10b-5. The ABA's Committee on Federal Regulation of Securities, *Report of the Task Force on Statute of Limitations for Implied Actions,* 41 Bus. Law. 645, 659-66 (1986), collects the decisions from around the circuits. Some states have more than one fraud or blue sky statute, complicating matters. States also revamp their laws more frequently than Congress amends the Securities Exchange Act. Illinois, for example, amended the statute of limitations in its blue sky act in 1985, and one of the questions with which the district court wrestled is the extent to which the alterations apply to a claim that accrued in 1977. (The district judge, disagreeing with four other district judges in the circuit, concluded that Short had at most two years after January 1, 1986, the effective date of the amendment. See also *Davenport,* 903 F.2d at 1141 n.5; *Norris,* 818 F.2d at 1333 n.*.) Translating state periods of limitations to federal court also has led to difficult questions concerning whose tolling and estoppel doctrines apply: the state's, the federal court's, or both? *Davenport, Norris,* and many other cases grapple

at length with the interaction of state and federal tolling rules.

Although this circuit regularly uses state blue sky laws, other circuits have been equally committed to different courses. From the perspective of practitioners litigating cases originating in many states (especially class actions), the situation is a nightmare. Lawyers and courts alike devote untold hours to identifying proper state analogies and applying multiple (conflicting or cumulative) tolling doctrines. "This uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of different parties litigating identical claims in different states. Neither plaintiffs nor defendants can determine their rights with any certainty. Vast amounts of judicial time and attorneys' fees are wasted." ABA Committee, 41 Bus. Law. at 647. Loud calls for reform issue from scholars and the bar. With a unanimity unmatched in any other corner of securities law, everyone wants a simpler way — and to everyone that means a uniform federal statute of limitations. In addition to the ABA Committee's plaint, see, e.g., Thomas Lee Hazen, 2 *The Law of Securities Regulation* § 13.8 (2d ed. 1990); Bateman & Keith, *Statutes of Limitations Applicable to Private Actions Under SEC Rule 10b-5: Complexity in Need of Reform,* 39 Mo. L. Rev. 165, 183 (1974); Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5,* 1973 Duke L.J. 1125, 1142; Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion,* 13 Wayne L. Rev. 637 (1967); Note, *Statutes of Limitation for Rule 10b-5,* 39 Wash. & Lee L. Rev. 1021 (1982). As Professor Loss puts it, *Fundamentals of Securities Regulation* 1168-69 (1983): "This reference to state law makes for a great amount of utterly wasteful litigation. . . . Would it not be eminently more consistent with the overall statutory scheme to look

to what Congress itself did when it was thinking specifically of private actions in securities cases than to a grab-bag of more or less analogous state statutes?"

Norris examined this subject and concluded that the statute of limitations in § 13 fits actions under Rule 10b-5 far more closely than the collection of statutes absorbed from state law. 818 F.2d at 1332-33. We did not jettison our existing approach, however, deeming it "too late for an inferior federal court to turn back the clock", 818 F.2d at 1333. When we decided *Norris*, the court of appeals were unanimous in thinking that state law supplies the statutes of limitations under Rule 10b-5. A month later the Supreme Court decided *Agency Holding*. Six months after that the third circuit broke ranks in *Data Access*, relying on *Agency Holding* and the analysis in *Norris*. Now that there is an established conflict among the circuits and the SEC has endorsed the use of federal law, we need not be so meek. Although *stare decisis* has its claims, *Agency Holding* took a bold step that invites the inferior federal courts to reconsider their handling of adjacent fields. We hold that federal and not state law supplies the statute of limitations in suits under § 10(b) and Rule 10b-5.*

We leave for the future all questions concerning retroactive application of this decision. Retroactivity has not been briefed, and the retroactive application of decisions affecting periods of limitations is a question of some subtlety depending on the nature of reliance interests. See *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971);

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*Because this decision changes a rule of law established in this circuit, effectively overruling cases that borrowed periods of limitations from state law, it was circulated to all judges in regular active service. See Circuit Rule 40(f). No judge voted to hear the case in banc.

St. Francis College v. Al-Khazraji, 481 U.S. 604 (1987); *Goodman v. Lukens Steel Corp.*, 482 U.S. 656, 662-64 (1987); *Hill v. Equitable Trust Co.*, 851 F.2d 691 (3d Cir. 1988) (applying *Data Access* retroactively); cf. *American Trucking Ass'ns, Inc. v. Smith*, 110 S. Ct. 2323, 2343-45 (Scalia, J., concurring), 2347-52 (Stevens, J., dissenting) (1990). It is enough for the moment to observe that new rules of law apply in the cases that establish them and that Short cannot have relied on Illinois law, because she claims to have been unaware of the basis for litigation until a short time before filing suit. Effects of reliance on our former holdings may be determined when the plaintiff demonstrates reliance.

B

Federal securities laws contain two candidate statutes of limitations. The first is § 13 of the Securities Act of 1933, as amended by the Securities Exchange Act of 1934, which provides:

> No action shall be maintained to enforce any liability under section 11 or section 12(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 12(1), unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 11 or section 12(1) more than three years after the security was bona fide offered to the public, or under section 12(2) more than three years after the sale.

Section 11 deals with errors and omissions in registration statements, including the portion of the registration

statement that circulates as the prospectus. Section 12(1) deals with sales "in violation of section 5" — that is, unregistered sales of securities required to be registered. Section 12(2) addresses all other forms of materially incorrect or misleading selling literature and oral communications in the sale of a security. *Data Access* selected § 13 as the appropriate federal law because misstatements and omissions that violate § 12(2) are the closest match to the subjects of Rule 10b-5. (Short could not have sued under § 12 itself; she complains of fraud by the buyer, while § 12(2) is addressed to fraud by the seller. Still, § 12(2) applies to the kind of conduct involved here.)

The second candidate is § 20A(b)(4) of the Securities Exchange Act of 1934, added by the Insider Trading and Securities Fraud Enforcement Act of 1988. This provides:

> No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

Section 20A(a) defines "the subject" as violating the '34 Act or its rules "by purchasing or selling a security while in possession of material, nonpublic information". The Solicitor General, representing the SEC in *Lebman*, asked the Supreme Court to use this statute for all actions under Rule 10b-5, on the rationale that inside trading violates Rule 10b-5, so that employing § 20A(b)(4) just extends it from some to all Rule 10b-5 actions.

Choosing between these statutes is difficult. Section 13 is attractive because it covers § 12(2), which describes the offense to which Rule 10b-5 is applied; fraudulent misstatements or omissions in connection with the purchase or sale of securities. Rule 10b-5 came into being when § 13 was the only game in town. Any court choosing a federal statute of limitations between 1946 (the date of

the first decision recognizing a private right of action under Rule 10b-5) and 1988 necessarily would have selected § 13. It is also the statute *Data Access* picked. To pick § 20A would be to create a fresh conflict among the circuits. Because a principal reason for choosing a federal law is to replace confusion with certainty, we are reluctant to depart from the statute that will be employed in the third circuit.

On behalf of § 20A one may say that five years represents Congress' latest thoughts and that because trading on material inside information violates Rule 10b-5, the *only* way to apply a single statute of limitations to all actions under that Rule is to use § 20A(b)(4). Clever lawyers could describe even a garden variety fraud as "purchasing or selling a security while in possession of material, nonpublic information — that is, the truth — blurring the line between the offenses and making the choice of a period of limitations difficult. Moreover, § 20A offers plaintiffs more time than does § 13. Section 10(b) and Rule 10b-5 require the plaintiff to prove scienter, which a plaintiff under § 12(2) need not; perhaps the additional years are appropriate to the extra requirements of litigation uner Rule 10b-5.

Interests in uniformity tug both ways: if we choose § 20A we shall have one statute of limitations for all Rule 10b-5 cases in the seventh circuit, but different rules in the seventh and third circuits. If we choose § 13 we shall be in line with the third circuit, but different kinds of claims under Rule 10b-5 will be subject to different periods of limitations. The latter diversity is likely to be tolerable. To obtain the five-year period of § 20A, the plaintiff would have to sue under § 20A, establish trading by an insider (Belleville Shoe's insiders did not trade with Short), and accept the limitations of that statute, including the restriction of damages to the defendants'

profit (as opposed to the plaintiff's loss). In the great bulk of cases, there will be no ambiguity.

One interest cuts strongly in favor of § 13: it is a statute of repose, while § 20A appears to be a statute of limitations. Section 13 gives one year from discovery, but "*[i]n no event* shall any such action be brought to enforce a liability created . . . under section 12(2) more than three years after the sale." (Emphasis added). Conduct by the defendant that postpones the date of discovery therefore does not extend the period of suit by more than two years. *Data Access* concluded that equitable tolling does not postpone the accrual of the claim, or equitable estoppel does not bar the invocation of § 13. See also *Admiralty Fund v. Hugh Johnson & Co.*, 677 F.2d 1301, 1308 (9th Cir. 1982); *Sumner v. Land & Leisure, Inc.*, 664 F.2d 965 (5th Cir. 1981); Bloomenthal, *Statutes of Limitations and the Securities Acts — Part I*, 7 Sec. & Fed. Corp. L. Rep. 18, 21 (1985) (collecting legislative history); ABA Committee, 41 Bus. Law. at 655. Cf. *Darms v. McCulloch Oil Corp.*, 720 F.2d 490 (8th Cir. 1983); *Aldrich v. McCulloch Properties, Inc.*, 627 F.2d 1036 (10th Cir. 1980) (both interpreting language in other statutes identical to § 13 as precluding any extension beyond three years).

Courts says that equitable tolling does not apply under § 13, see Hazen, *1 Law of Securities Regulation* § 7.5.4 at 340-42 (collecting cases), but this is not strictly accurate. It is better to say that equitable tolling and related doctrines do not extend the period of limitations by more than the two-year grace period § 13 allows. *Norris*, 818 F.2d at 1332. Congress did not obliterate these valuable doctrines so much as it set bounds on the length of delay. It may be that equitable estoppel could preclude resort to the one-year period after discovery, even though no tolling of the three-year outer limit is possible; we need not

decide. Unless the "in no event more than three" language cuts off claims of tolling and estoppel at three years, however, it serves no purpose at all — what other function could be served by such language in a statute that starts the time on discovery?

Section 20A, by contrast, appears to be an ordinary statute of limitations. The SEC believes that it is a statute of repose as well as a statute of limitations, see *Lebman* amicus brief at 14 n.17, but it is not so clear to us. The language is in the traditional form of a statute of limitations, and the Solicitor General did not cite any legislative history indicating that it is more potent than the usual variety. (No case has been decided under the period of limitations established in § 20A, and none is likely to be until after 1993.)

The difference between statutes of limitations and statutes of repose is substantial in securities litigation. Indeed, the SEC's submission that § 20A should be used across the board appeared to depend on its conclusion that § 20A, like § 13, is a statute of repose. All of the express provisions in the '33 and '34 Acts (other than § 20A), are drawn as statutes of repose, and deliberately so. Prices of securities are volatile. If suit may be postponed indefinitely on equitable grounds, then investors may gamble with other people's money. An investor in Short's position may sell her shares for a price certain. If the firm does poorly, she keeps the money; if it does well, she sues and asks for the increase in value. Congress chose one year after discovery, and a cap of two additional years on tolling principles, in order to curtail the extent to which the securities laws permit recoveries based on the wisdom given by hindsight. This was why in 1934 Congress repealed the period in the original version of the '33 Act (two years from discovery, and in no event

more than ten) and replaced it with the current § 13 (one year from discovery, and in no event more than three). See H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. 32, 36, 42 (1934); 78 Cong. Rec. 8198-8203 (May 7, 1934) (Senate amendments carried to the conference); J.S. Ellenberger & Ellen P. Mahar, 6 *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934* 6565-66, 6718, 6993 (1973), and 7 *id.* at 7743-44. Investors then have a more powerful incentive to investigate rather than accept another person's word without question, as Short says she did. Prudent investors almost always can sniff out fraud (or enough smoke to justify litigation) within three years. Section 13 cuts off only the claims of the most trusting or somnolent — or the most wily, those who wanted to wait as long as possible.

Setting an outer limit for claiming fraud or material omissions in the sale of securities is an important aspect of § 13, one of the principal reasons Congress designed the statute that way. Section 20A, by contrast, uses for inside trading cases a measure of damages that the passage of time does not affect. Section 20A(b)(1) provides that the "total amount of damages . . . shall not exceed the [insider's] profit gained or loss avoided in the transaction or transactions that are the subject of the violation." Profit gained or loss avoided is a contemporaneous measure: the difference between the price the insider realizes and the market price of the securities after the news is released. *Wisconsin Real Estate Investment Trust v. Weinstein*, 781 F.2d 589, 596-97 (7th Cir. 1986); *SEC v. MacDonald*, 699 F.2d 47, 52-55 (1st Cir. 1983) (in banc); *Gerstle v. Gamble-Skogmo, Inc.*, 478 F.2d 1281, 1306 n.27 (2d Cir. 1973) (Friendly, J.). This sum is fixed within days after the trading, sometimes within hours. No one has a free put or call of securities; no one can use delay in bringing suit to speculate on the firm's future

prosperity. Section 20A may use a five-year period, and be drafted as an ordinary statute of limitations, precisely because the reasons for setting the shorter one-and-three period for fraud are not present. To select § 20A(b)(4) as the rule for *all* Rule 10b-5 actions, just because a five-year period has been deemed appropriate for one atypical kind of violation, would let the tail wag the dog. Congress did not say that § 20A applies to all cases under Rule 10b-5; it did not amend § 13; it limited the scope of § 20A's statute of limitations to a particular and atypical kind of violation. Section 20A(b)(4) has been prescribed for inside trading cases; run-of-the-mine frauds under Rule 10b-5 should be governed by the statute in force when Rule 10b-5 came into being, the statute *designed for* the kind of conduct about which Short and most other 10b-5 plaintiffs complain: § 13 of the Securities Act of 1933.

Application of § 13 to this case is straightforward. Short sold her shares to Belleville Shoe on May 5, 1977. Although she contends that she did not discover the fraud until late 1988, the second sentence of § 13 sets three years after the sale as the outer limit for litigation. That time expired in 1980. Suit was not filed until 1989. It is untimely.

II

Short's second federal claim arises under RICO. She contends that Belleville and the other defendants carried out a pattern of racketeering acts (that is, of securities fraud) by acquiring the stock of four minority investors in 1977. Short, Louise Lampert Larsen, and Jean Lampert Sundheim sold their stock in spring 1977, and Rosalind Wagner that fall. These sales, according to Short, establish a "pattern" of fraud characterized by the necessary

"continuity plus relationship", *H.J. Inc. v. Northwestern Bell Telephone Co.*, 109 S. Ct. 2893, 2900 (1989). The district court disagreed, holding that four transactions in close proximity 12 years ago do not establish the "continuity" element in the absence of a threat of enduring fraud.

We approach the question with diffidence, because "continuity plus relationship" is such an ambulatory phrase. Still, it it impossible to stretch the events of 1977 into a "pattern" of fraud. Belleville Shoe's board of directors authorized the purchases at a price of $273 per share in a single resolution, dated May 1, 1977. The four investors accepted Belleville Shoe's offer at different times — Wagner accepting in the fall because she was out of the country when the other three said yes. One offer followed by four acceptances hardly threatens "continuity" of any kind. The Court said in *H.J.* that "[p]redicate acts extending over a few weeks or months and threatening no future criminal conduct do not satisfy this [continuity] requirement." 109 S. Ct. at 2902. This language supplied the basis of the holding in *Sutherland v. O'Malley*, 882 F.2d 1196 (7th Cir. 1989), that a course of conduct stretching over five months did not amount to "continuity". See also *Management Computer Services, Inc. v. Hawkins, Ash, Baptie & Co.*, 883 F.2d 48 (7th Cir. 1989).

Short tries to rescue her case by characterizing the threat of further misconduct against minority shareholders as the source of continuity. She does not identify any such investors, however, or explain how they were threatened. The complaint does not mention any further purchases of stock under circumstances suggesting fraud. RICO is not designed to transfer to federal court all claims of oppression of minority investors in violation of

fiduciary duties established by corporate law. Short may pursue such contentions in state court; all of her claims under state law were properly dimissed, for lack of an independent jurisdictional basis, following the failure of her two federal claims. Short insists that Illinois' tolling rules would allow her to recover from Belleville Shoe and her relatives 13 years after the events. She may test that belief in the appropriate forum.

AFFIRMED

POSNER, *Circuit Judge*, concurring. I have no disagreement with the court's opinion or judgment, and join both, writing separately only to express reservations about the principle of "borrowing" a period of limitations from one statute for use with another (here, a rule of the SEC, but the principle is the same) that has none. The Supreme Court's unwavering attachment to the principle leaves us no choice but to apply it, but that attachment is beginning to be questioned, *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143, 157-70 (1987) (concurring opinion), and I would like to add my small voice to the chorus.

Borrowing a period of limitations from one statute to use with another that doesn't have its own limitations provision is a matter of which round peg to stuff in a square hole. It artificially truncates the court's choice of an *appropriate* period, one well suited to the *particular* statute under consideration. It also runs the risk of applying one unprincipled legislative deal to a problem entirely outside the scope of the deal. Suppose Statute A specifies no period of limitations. Statute B regulates analogous conduct, and has a six-month period. But maybe B has such a short deadline for suit only because the interest group that opposed the enactment of B had enough muscle to block a longer deadline that would have

made more sense from a neutral standpoint. In that event, to borrow B's limitations period for use with A will project the interest-group pressures that deformed B into a completely new area of conduct.

Whether or not courts are aware of this danger, they do attempt to correct for it by considering, as part of the borrowing procedure, the suitability to the substantive rule under consideration of the limitations periods in the various candidate statutes of limitations. But this places a lot of balls in the air. The considerations bearing on the suitability of one limitations period over another include the difficulty of investigating potential violations, the possibility that the consequences of wrongdoing will be delayed, the opportunities for wrongdoers to conceal the wrong, the rate at which evidence of wrongdoing and also evidence pertinent to the alleged wrongdoer's defenses is likely to decay, the sophistication of the relevant tribunals in handling stale evidence, the desirability of freeing court time for fresh claims, the interest of potential defendants in repose — that is, in knowing after a definite period has passed that they no longer have to worry about being sued — and the effect on the deterrence of statutory violators of reducing the time for bringing suit. When these considerations are mingled with the underlying question of the similarity between the conduct in the case at issue and the conduct to which the various candidate statutes of limitations apply, we have the essential condition for standardless, discretionary judgment: a multi-factor test with no weights on the factors. Since courts cannot be expected to converge on a uniform outcome when they are operating under such a standard, predicting what statute of limitations will be borrowed is impossible and as a result extensive litigation often is necessary before a definitive conclusion on the limitations period emerges. It may not come until a Supreme Court

decision is rendered resolving an intercircuit conflict that was years in the brewing.

As we noted in *Hemmings v. Barian*, 822 F.2d 688, 689 (7th Cir. 1987), judges feel that they have to borrow an existing statute of limitations rather than lay down a period of limitations as a matter of federal common law because it would be arbitrary to pick a term of years. They feel in other words that enactment of a limitations period, because of its inescapable arbitrariness, is a legislative rather than a judicial task. Legislators can be as arbitrary as they please within the broad limits set by the Constitution but judges are supposed to reason to their conclusions, and how can you *reason* to 3 years over 2, 300 days over 240, 20 years over 15? You cannot; but neither can you reason to the right statute of limitations to borrow. The imponderables are so numerous that in the end the borrowing judgment, too, is inescapably arbitrary, as the present case illustrates.

What is to be done? There are several possibilities. One would be for courts to drop the mask and create statutes of limitations for claims that lack them. There is precedent for this in the judicial doctrine of laches, which on at least one occasion was firmed up into a period of definite length. *Smith v. City of Chicago*, 769 F.2d 408 (7th Cir. 1985). Yet even then we borrowed the limitations period in an existing statute. The difficulty with creating a statute of limitations *ex nihilo* lies in the fact that judge-made rules come in the first instance from the bottom of the judicial hierarchy, rather than being imposed from on high. In the early days of a new substantive statute that specified no limitations period, each district judge would be selecting a period of limitations for the individual case, each court of appeals would be selecting the period for the case in the circuit, and only when the Supreme Court got

a case would the definitive period finally be declared. The improvements over the borrowing procedure would be modest; they would be chiefly in the area of judicial candor.

An institutional solution is necessary, and two possibilities come to mind. One, which wouldn't work in this case because the cause of action postdates the enactment of the statute under which it arises, would be for Congress to adopt a rule that every statute shall contain a statute of limitations. This course would be superior to Congress's adopting (as sometimes proposed) a general catch-all statute of limitations, because there is no single period of limitations tht would be suitable for the entire range of causes of action in statutes that do not specify a period. Such a rule might, it is true, be ineffectual without a nagging agency within Congress to enforce it, some counter-part to the Congressional Budget Office, as proposed in the Report of the Federal Courts Study Committee 21-22, 89-93 (April 2, 1990) — unless the Supreme Court adopted Justice Scalia's view that if a statute contains no period of limitations, there just is no deadline on suing. *Agency Holding Corp. v. Malley-Duff & Associates, Inc., supra,* 483 U.S. at 164. This would cause considerable havoc but could be mitigated by a rule (well within the power of judges to create, I believe) that, in the absence of a statutory limitations period, the courts will apply the equitable doctrine of laches even if the cause of action is legal rather than equitable. Then the defendant could defend by showing that the plaintiff had unreasonably delayed in bringing the suit and that the defendant had been hurt by the delay. There is precedent for applying laches in cases at law. *Piper Aircraft Corp. v. Wag-Aero, Inc.,* 741 F.2d 925, 939 (7th Cir. 1984) (concurring opinion).

The second institutional possibility would be for Congress to delegate to the Judicial Conference of the United States, or to some new agency modeled on the Sentencing Commission — perhaps my hypothetical "nagging agency" — the power to adopt by regulation a period of limitations for any statute that does not have one. This would lift the burden from Congress of having to specify a limitations period in every enactment and would shift it to an expert body that could avoid the delay of litigation. It would be a great improvement over borrowing.

A true Copy:
Teste:

Clerk of the United States Court of Appeals for the Seventh Circuit

Supreme Court, U.S.
FILED
DEC 5 1990
JOSEPH F. SPANIOL, JR.
CLERK

(4)

No. 90-333

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ, and
ANTHONY CATALAN, *et al.*,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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JOINT APPENDIX

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Petition for Writ of Certiorari Filed August 10, 1990
Writ of Certiorari Granted October 9, 1990

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* The remaining opinions and orders of the District Court and the Court of Appeals relevant to the proceedings in this Court are printed in the appendix to the petition for writ of certiorari and therefore have not been reproduced herein.

RELEVANT DOCKET ENTRIES IN THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

No. 88-4100

JOHN GILBERTSON and JANICE GILBERTSON, *et al.*
Plaintiffs-Appellants,

v.

ANDERS G. ARNHEIM; ALANTHUS CORPORATION, formerly known as Technology Finance Group, Inc.; COMPUTER VALUE ASSOCIATES; AMERICAN COMPUTER EQUIPMENT LEASING; LEASING CONSULTANTS ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; WILLIAM MCKENNA; TEXCOM EQUIPMENT CORPORATION; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, *et al.*,
Defendants-Appellees.

No. 88-4077

JOHN V. REITZ; JUDITH MACDONALD; DALE R. PETERSON; EARL D. RIDDLE; JACK E. EVANS; HARLAN C. SELBY; ROBERT E. JOHNSEN; PERRY COLEMAN; NICKOLAS J. MADESH; ROBERT A. GRAHAM; JERRY E. MARKS, *et al.*,
Plaintiffs-Appellants

v.

LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D.

WELLBROCK; WILLIAM B. WARD, *et al.*,; GLOBAL COMPUTER CORPORATION; RONALD JOHNSON; TEXCOM EQUIPMENT CORPORATION; COMDISCO, INC.; KENNETH M. PONTIKES; MARTIN KARNOFF; JOHN COSTELLO; DAVID MARKS; GORDON S. ROSEN ASSOCIATES, INC.; GORDON S. ROSEN; SOFTWARE SYSTEMS FOR WORD PROCESSORS, INC.; BERLENT INDUSTRIES, INC.; HARVEY BERLENT

Defendants-Appellees

No. 88-4099

ANTHONY E. CATALAN,

Plaintiff-Appellant,

v.

PAULSON INVESTMENT COMPANY, INC.; LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW; COMPUTER VALUE ASSOCIATES; GORDON S. ROSEN ASSOCIATES, INC.; TECHNICAL MARKETING SERVICES, INC.; LEASING CONSULTANTS ASSOCIATES; WILLIAM MCKENNA; RICHARD A. HEITMEYER; RICHARD D. WELLBROCK; WILLIAM B. WARD, *et al.*,

Defendants-Appellees

9/21/88 Filed order (Deputy Clerk: AHH) appellants' motion to consolidate appeals No. 88-4077, 88-4099 and 88-4100 is granted [1191606-1] in 88-4099, 88-4077, 88-4100 [88-4099, 88-4077, 88-4100] (mt) [88-4077, 88-4099, 88-4100]

2/8/89 Filed original and 15 copies Appellant John V. Reitz in 88-4077, Appellant Judith MacDonald in 88-4077, Appellant Dale R. Peterson in 88-4077, Appellant Earl D. Riddle in 88-4077, Appellant Jack E. Evans in 88-4077, Appellant Harlan C.

Selby in 88-4077, Appellant Robert E. Johnsen in 88-4077, Appellant Perry Coleman in 88-4077, Appellant Nickolas J. Madesh in 88-4077, Appellant Robert A. Graham in 88-4077, Appellant Jerry E. Marks in 88-4077, Appellant Anthony E. Catalan in 88-4099, Appellant John Gilbertson in 88-4100, Appellant Janice Gilbertson in 88-4100 opening brief 68 pages, and five excerpts of record in 4 volumes; served on 2/6/89 (per confatt) [88-4077, 88-4099, 88-4100] (tsp) [Entry date 02/09/89] [88-4077, 88-4099, 88-4100]

4/12/89 Received orig. copies 15 Lampf, William McKenna, Leasing Consultants, et al's brief of 91 pages and 5 excerpts; served on 4/10/89 [Brief returned to counsel for correction of double-sided printing; excerpts on shelf] [88-4077, 88-4099, 88-4100] (dmf) [Entry date 04/13/89] [88-4077, 88-4099, 88-4100]

4/26/89 Filed original and 15 copies appellee Anders G. Arnheim, et al in 88-4100's 19 pages brief, 0 Exc. vols:; served on 4/24/89 [88-4077, 88-4099, 88-4100] (dmf) [88-4077, 88-4099, 88-4100]

4/27/89 Filed original and 15 copies appellee Kenneth M. Pontikes, Comdisco, Inc.'s 24 pages brief, 1 Exc. vols:; served on 4/24/89 [88-4077, 88-4099, 88-4100] (dmf) [88-4077, 88-4099, 88-4100]

5/25/89 Filed original and 15 copies John V. Reitz, et al's joint reply brief, 46 pages, served on 5/22/89 [88-4077, 88-4099, 88-4100] (dmf) [Entry date 05/26/89] [88-4077, 88-4099, 88-4100]

9/12/89 ARGUED AND SUBMITTED TO: PREGERSON, TROTT, FERNANDEZ [88-4077, 88-4099, 88-4100] (pg) [Entry date 09/18/89] [88-4077, 88-4099, 88-4100]

2/5/90	FILED MEMORANDUM OPINION: We REVERSE AND REMAND for proceedings consistent with our holdings herein. (Terminated on the Merits after Oral Hearing; Reversed; Written, Unsigned, Unpublished. PREGERSON, TROTT, author; FERNANDEZ) FILED AND ENTERED JUDGMENT. [88-4077, 88-4099, 88-4100] (jr) [Entry date 02/22/90] [88-4077, 88-4099, 88-4100]
2/20/90	[1718945] Filed original and 40 copies aples' (Lampf, Pleva, et al) petition for rehearing with suggestion for rehearing en banc 13 pages; served on 2/16/90 to (PANEL & ALL ACTIVE JUDGES). [88-4077, 88-4099, 88-4100] (jr) [Entry date 02/22/90] [88-4077, 88-4099, 88-4100]
5/16/90	Filed order (PREGERSON, TROTT & FERNANDEZ) the petition for rehearing is DENIED and the suggestion for rehearing en banc is REJECTED. [1718785-1] in 88 4077, 88-4099, 88-4100 [718945-1] in 88-4077, 88-4099, 88-4100 [88-4077, 88-4099, 88-4100] (jr) [88-4077, 88-4099, 88-4100]
7/13/90	MANDATE ISSUED. COSTS TAXED. [88-4077, 88-4099, 88-4100] (dmf) [88-4077, 88-4099, 88-4100]
8/29/90	Rec'd notice from Supreme Court: petition for certiorari filed on 8/10/90, Supreme Court No. 90-333. [88-4077, 88-4099, 88-4100] (jr) [Entry date 09/11/90] [88-4077, 88-4099, 88-4100]

RELEVANT DOCKET ENTRIES IN THE UNITED STATES DISTRICT COURT FOR THE DISTRICT OF OREGON

Civ. 86-1368-RE

JOHN REITZ, *et al.*
v.
LEASING CONSULTANTS ASSOCIATES, *et al.*

1986		
Nov. 3	1)	COMPLT-sec. law violation
Dec. 5	5)	FIRST AMENDED COMPLT with J/T demand
1987		
Mar. 13	146)	2nd AMENDED COMPLT with J/T demanded
Mar. 17	148)	ORD- discv open only on the issues of the statute of limitations, venue & pers. jurisd ***
May 6	214)	3rd AMENDED COMPLT-j/t demanded
Aug. 3	288)	4th AMENDED COMPLT; j/t demanded
Oct. 1	319)	ANS of LCI, Inc. Leasing Consultants Assoc. Wm. L. McKenna & Richard Wellbrock to 2nd am/complt, cross claims & am/3rd party complt; j/t demand

1988

Feb. 1	399)	Deft Lampf's mot for s/j
Feb. 1	400)	Certain defts' joint memo in support of mots for s/j
Feb. 1	401)	Affidvt of R. Daniel Lindahl in support of certain defts' mot for s/j
Feb. 1	403)	Affidvt of Elizabeth Chadwick as to serv on 3rd party deft James D. Quenemoen
Feb. 1	404)	Affidvt of Elizabeth Chadwick as to serv on 3rd party deft R.G. Williams
Feb. 1	409)	Deft Lampf's mot for s/j
Feb. 1	410)	Exhibits A-D to the affidvt of R. Daniel Lindahl
Feb. 1	411)	Exhibits E-L to the affidvt of R. Daniel Lindahl
Feb. 1	412)	Exhibits M-N to the affidvt of R. Daniel Lindahl
Feb. 1	413)	Exhibits O-Q to the affidvt of R. Daniel Lindahl
Feb. 1	414)	Exhibits R-S to the affidvt of R. Daniel Lindahl
Feb. 1	415)	Exhibits T-V to the affidvt of R. Daniel Lindahl
Feb. 22	428)	Troy assoc. pltfs' response to mots for s/j
Feb. 22	429)	Affidvt of Robert L. Halloran in response to defts' mots for s/j
Feb. 22	430)	Lamar Assoc. pltfs' response to mots for s/j

Feb. 22	431)	Salem Assoc. pltfs' response to mots for s/j
Feb. 22	432)	Euston pltfs' response to defts' mots for s/j
Feb. 22	433)	Duval pltfs' response to defts' mots for s/j
Feb. 22	434)	Mt. Hood pltfs' response to defts' mots for s/j
Feb. 22	435)	Columbia assoc. pltfs' response to mots for s/j
Feb. 22	436)	Pltfs' joint memo in opposit to all defts' mots for s/j; o/a req.
Feb. 22	437)	Affidvt of Justine Fischer
Feb. 22	439)	Exhibit A to O'Halloran affidvt in response to defts' mots for s/j
Feb. 22	440)	Exhibit B to O'Halloran affidvt in response to defts' mots for s/j
Feb. 22	441)	Exhibits C through OO to O'Halloran affidvt in response to defts' mots for s/j
Mar. 4	449)	Deft Lampf's memo in reply to pltfs' opposit to lampf's mot for s/j
Mar. 4	450)	Affidvt of Cindy Zemaitis
Mar. 4	452)	Lci defts reply to pltfs' opposit to defts' mots for s/j
Mar. 4	453)	Affidavit of David A. Urman
Mar. 21	457)	Rec of hrg- ord taking u/advise
Mar. 24	458)	Rec of ord: Discv & all proceedings in case are placed on stay until issuance of the opinion and ord on defts' mot for s/j on statute of limitation grounds

Jun. 13	462)	OPINION-Only the orico claims remains. I decline to exercise pendent jurisd. over this state claim & dism it for want of subj. matter jurisd-in Catalan. Granting defts' mots for s/j.e/7-13 s/7-13 RE ntfd
Jan. 13	463)	ORD- all defts' mots for s/j are granted. SO ord. e/7-13 s/7-13 RE ntfd
Jun. 14	465)	JDGMT- for defts & cases are dism. e/7-15 s/7-14 RMC, clerk ntfd
Aug. 10	480)	NOTC OF APPEAL Pltfs from judgment 7/14/88

Civ. 86-1369-RE

JOHN B. GILBERTSON AND JANICE GILBERTSON
v.
LEASING CONSULTANTS ASSOCIATES, *et al.*

1986

Nov. 3	1)	COMPLT-Sec. law violation with J/T demanded
Dec. 1	6)	AMENDED COMPLT-with J/T demanded

1987

Mar. 13	244)	2nd AMENDED COMPLT- J/T demand
17	250)	ORD-discv open only on the issues of the statute of limitations, venue & pers. jurisd.
		* * *
20	251)	Pltfs' mot for leave to file 3rd am/complt
Apr. 3	264)	Rec of ord granting pltfs' mot for leave to file 3rd am/complt.
Jul. 23	403)	4th AMENDED COMPLT; j/t demanded
Oct. 1	434)	ANS of LCI, Inc. Leasing Consultants Assoc. Wm. McKenna & Richard Wellbrock to 2nd am/complt, cross-claims & am/3rd party complt; j/t demanded

1988

Feb. 1	500)	Mor of defts Arnheim, MCCostis, Hurwitz & Schreiber for s/j with o/ a req
Feb. 1	501)	Memo in support
Feb. 1	502)	Affidvt of Richard A. Wyman in support
Feb. 1	503)	Exhibits of defts in support of their memo
Feb. 1	(())	Deft Lampf's mot for s/j
Feb. 1	(())	Certain defts' joint memo in support of mots for s/j
Feb. 1	(())	Affidvt of R. Daniel Lindahl in support of certain defts' mot for s/j
Feb. 1	(())	Affidvt of Elizabeth Chadwick as to serv on 3rd party deft James D. Quenemoen
Feb. 1	(())	Affidvt of Elizabeth Chadwick as to serv on 3rd party deft R.G. Williams
Feb. 1	(())	Deft Lampf's mot for s/j
Feb. 1	(())	Exhibits A-D to the affidvt of R. Daniel Lindahl
Feb. 1	(())	Exhibits E-L to the affidvt of R. Daniel Lindahl
Feb. 1	(())	Exhibits M-N to the affidvt of R. Daniel Lindahl
Feb. 1	(())	Exhibits O-Q to the affidvt of R. Daniel Lindahl
Feb. 1	(())	Exhibits R-S to the affidvt of R. Daniel Lindahl

Feb. 1	(())	Exhibits T-V to the affidvt of R. Daniel Lindahl
Feb. 1	505)	Exhibits to memo in support of mot for s/j of deft Comdisco & Kenneth N. Pontikes
Feb. 1	506)	Memo in support of mot for s/j of deft Comdisco & Kenneth Pontikes

1988

Feb. 22	525)	Troy assoc. pltfs' response to mots for s/j
Feb. 22	526)	Affidvt of Robert L. O'Halloran in response to defts' mots for s/j
Feb. 22	528)	Lamar Assoc. pltfs' response to mots for s/j
Feb. 22	529)	Salem assoc. pltfs' response to mots for s/j
Feb. 22	530)	Euston pltfs' response to defts' mots for s/j
Feb. 22	531)	Duval pltfs' response to defts' mots for s/j
Feb. 22	532)	Mt. Hood pltfs' response to defts' mots for s/j
Feb. 22	533)	Columbia assoc. pltfs' response to mots for s/j
Feb. 22	534)	Pltfs' joint memo in opposition to all defts' mots for s/j
Feb. 22	535)	Affidvt of Justine Fischer
Feb. 22	(()	Exhibit A to O'Halloran affidvt in response to defts' mots for s/j
Feb. 22	(()	Exhibit B to O'Halloran affidvt in response to defts' mots for s/j

Feb. 22	(()	Exhibits C through OO to O'Halloran affidvt in response to defts' mots for s/j
Mar. 4	541)	Deft Lampf's memo in reply to pltfs' opposit to lampf's mot for s/j
Mar. 4	542)	Affidvt of Cindy Zemaitis
Mar. 4	544)	Affidvt of Richard A. Wyman in support of Amh&s reply brief (statute of Limit)
Mar. 4	545)	Defts Arnheim, McCostis, Hurwitz & Schreiber's reply memo
Mar. 4	548)	Reply memo in support of the mot for s/j of defts Comdisco, Inc & Kenneth Pontikes
Mar. 4	549)	2nd affidvt of Caryn Jacobs
Mar. 4	550)	Lci defts' reply to pltfs' opposit to defts' mots for s/j
Mar. 4	551)	Affidvt of David A. Urman
Mar. 21	553)	Rec of hrg- ord taking u/advise
Mar. 24	553A)	Rec of ord-Discv & all proceedings in case are placed on stay until issue of the opinion & ord on defts' mot for s/j on statute of limitation
Jul 13	555)	OPINION- only the orico claims remains [sic]. I decline to exercise pendent jurisd. over this state claim & dism it for want of subj. matter jurisd. in Catalan. Granting defts' mots for s/j. e/7-13 s/7-13 RE ntfd
13	556)	ORd- all defts' mots for s/j are granted. SO ORd. e/7-13 s/7-13 RE ntfd

14	557)	JDGMT- is for defts & these cases are dism. e/7-15 s/7-14 RMC, clerk ntfd
Jul 10	567)	NOTC OF APPEAL pltfs from judgment 7/14/88

Civ. 87-593-RE

ANTHONY E. CATALAN
v.
PAULSON INVESTMENT CO., *et al.*

1987			
June 4	1)	Complnt (securities law violations, RICO, Common Law Fraud, Negligence)	
Oct. 15	73)	First a/mended complaint	
1988			
Feb. 1	151)	Deft Lampf's mot for S/J	[c-RE]
Feb. 1	153)	Certain Defts' Joint Memo in support of mots for S/J	[c-RE]
Feb. [1	153c)	Affid of R. Daniel Lindahl in support of certain Defts mots for S/J	[c-RE]
Feb. 22	())	Exh A to O'Halloran affid in response to defts' mots for S/J	[to RE]
Feb. 22	())	Exh B to O'Halloran affid in response to defts' mots for S/J	[to RE]

Feb. 22	())	Exh C through OO to O'Halloran affid in response to defts' mots for S/J	[to RE]
Feb. 22	162)	Pltfs' joint memo in opposn to all defts' mots for S/J o/a reqstd	[to RE]
Feb. 22	163)	Columbia Assoc Pltfs' response to mots for S/J	[to RE]
Feb. 22	164)	Mt Hood Pltfs' response to Defts' mots for S/J	[to RE]
Feb. 22	165)	Duval Pltfs' response to Defts' mots for S/J	[to RE]
Feb. 22	166)	Euston Pltfs' response to Defts' mots for S/J	[to RE]
Feb. 22	167)	Troy Assoc Pltfs' response to mots for S/J	[to RE]
Feb. 22	168)	Salem Assoc Pltfs' response mots for S/J	[to RE]
Feb. 22	169)	Affid of Anthony E. Catalan	[to RE]
Feb. 22	170)	Affid of Justine Fischer	[to RE]
Feb. 22	171)	Affid of Robt L. O'Halloran in response to Defts' mots for S/J	[to RE]
Feb. 22	173)	Lamar Assoc Pltf's response to mots for S/J	[to RE]

Mar. 4	178)	Deft Lampf's memo in srply to pltfs' opposn to Lampf's mot for S/J [to RE]
Mar. 4	179)	Affid of Cindy Zemaitis [to RE]
July 13	186)	OPN-I grant defts' mots for s/j s RE 7/13/88 e/m 7/13/88 ntfd
July 13	187)	ORD-ORD that all of defts' mots for s/j are granted. s RE 7/13/88 ntfd
July 14	188)	JUDGMENT-ORD that judgment is for defts & these three cases are dsmsd
Aug. 10	193)	NOTICE OF APPEAL-Notice is hereby given that pursuant to Ruel [sic]4(a), Federal Rules of Appellate Procedure, pltf hereby appeals to the U.S. Court of Appeals for the Ninth Circuit from the jdgmnt entered on 7-14-88, dismissing this action, and the order entered on 7-13-88, granting defts' mots for s/j.

COMPLAINT IN *REITZ, et al.* V. *LEASING CONSULTANTS ASSOCIATES, et al.*, Civ. No. 86-1368-RE (D. ORE.)
(EXCERPTS)

• • •

Plaintiffs allege:

ALLEGATIONS COMMON TO ALL CLAIMS FOR RELIEF
JURISDICTION AND VENUE

1. Count I of each Claim for Relief asserted herein arises under Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)(1). Jurisdiction for these Counts is conferred by 15 U.S.C. § 77v. Count II of each Claim for Relief asserted herein arises under Section 10 of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j and 17 C.F.R. 240.10(b)-5. Jurisdiction for these Counts is conferred by 15 U.S.C. § 78aa. Counts IV, V and VI of each Claim for Relief asserted herein arise under the Racketeer Influenced and Corrupt Organizations Act of 1970 ("RICO"), 18 U.S.C. §§ 1962 and 1964. Jurisdiction for these Counts is conferred by 18 U.S.C. §§ 1964 and 1965. Jurisdiction for Counts III and Counts VII through XI of each Claim for Relief asserted herein arises under the principles of pendent jurisdiction.

2. Venue is proper in this district in that the acts alleged herein took place in whole or in part in Oregon, including the sales of the securities described herein, and the plaintiff's claims arose in this district.

DESCRIPTION OF THE PROGRAMS

3. This action arises out of the packaging, syndication, promotion and sale in Oregon of certain tax shelter limited partnerships known as Duval Associates, LaMar Associates, Mt. Hood Associates, Columbia Associates, Salem Associates, and Euston Associates. As more particularly described herein, these tax shelters involved the purchase and leaseback of certain IBM computer hardware equipment and certain so-called master tapes of computer soft-

ware programs. Plaintiffs invested in these tax shelters by purchasing limited partnership units in one or more of these partnerships.

4. These tax shelter partnerships were promoted and sold during 1979, 1980, and 1981 to general partners and then to investors as "pre-packaged" programs. The partnerships were identical or virtually identical to each other in several respects, including the following:

a. Each partnership was packaged and promoted by the same group of six defendants ("the packagers"), as described more particularly herein.

b. Each partnership was comprised of 35 limited partnership "units" and was designed to raise approximately $1 million.

c. Each partnership was to enter into identically structured sale and leaseback transactions with respect to the computer equipment and master tape, as described more particularly herein.

d. Each partnership was created as a Connecticut limited partnership.

e. The offering memoranda used to promote and sell the partnerships were virtually identical in format and in content.

f. The tax opinions contained in these offering memoranda were virtually identical in format and in content.

g. The equipment appraisals contained in these offering memoranda were virtually identical in format and contained a substantial number of identical or virtually identical phrases.

h. The master tape appraisals contained in these offering memoranda were similar in format and contained a substantial number of identical or virtually identical phrases.

5. These partnerships were also similar to at least twelve other tax shelter limited partnerships packaged and promoted by the packager defendants in Oregon and elsewhere during this same time period, including the limited partnerships known as Troy Associates, Runnels Associates, Lake Associates, Mars Associates, Victoria Associates, Travis Associates, K-T Associates, Bandera Associates, Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum Associates.

6. The tax benefits purportedly to be derived from investing in the limited partnerships described herein were to be achieved through a complex series of purchase, sale and leaseback transactions structured and arranged by the packager defendants. As described in the offering memoranda used to promote and sell the investments, these transactions were to be structured as follows:

a. The Equipment Transactions

(1) Each partnership was to purchase certain specified IBM computer hardware equipment (the "equipment") from an identified entity. This entity was the immediate seller of the equipment to the partnership and will hereinafter be referred to as the "immediate seller." The partnership was to pay less than ten percent of the purchase price of the equipment in cash at closing, and the remainder was to be financed by a nine-year nonrecourse note. The equipment was purportedly already subject to a bank debt at the time of this transaction.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the equipment from another identified entity (the "equipment seller") for resale to the partnership.

(3) Simultaneously with purchasing the equipment from the immediate seller, the partnership was to lease the equipment back to the equipment seller under a noncancellable nine-year lease. The equipment seller would

thereby become a lessee of the equipment from the partnership. This entity will hereinafter be referred to as the "equipment seller/lessee."

(4) At the time of all these transactions, the equipment was represented to be already in place and in use by one or more identified nationally recognized companies (the "user"). The user had purportedly leased the equipment from the equipment seller/lessee before it was sold to the immediate seller for resale to the partnership. This underlying lease (the "user lease") was to expire within 36 to 48 months, at which time the equipment was to be re-leased to another user, if possible. During the pendency of any such subsequent user lease, the partnership was to receive a specified "bonus rental" of approximately 50 percent of the subsequent user's lease payments.

b. The Master Tape Transactions

(1) In addition to and simultaneously with purchasing the computer equipment, each partnership was to also purchase a master tape for certain specified computer software (the "master tape") from the same immediate seller from whom it had purchased the computer equipment. The master tape was purportedly designed for a specialized function or for use in a specific identified industry, and was purportedly readily marketable for that function or within that industry. The partnership was to pay less than ten percent of the purchase price of the master tape in cash at closing, and the remainder was to be financed by a long-term note of approximately 20 years. In addition, each partner in the partnership was to execute a "personal liability agreement" making him or her personally liable for his or her pro-rata share of the partnership's liability on the master tape note.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the master

tape from another identified entity (the "master tape seller") for resale to the partnership.

(3) Simultaneously with purchasing the master tape from the immediate seller, the partnership was to lease the master tape back to an identified affiliate of the master tape seller. This entity will hereinafter be referred to as the "master tape lessee."

(4) The master tape lessee was to market and license the master tape to businesses or entities that were in need of the specialized function the software could perform or within the specific industry for which the software was designed. Revenues generated from marketing and licensing the master tape were to be shared with the partnership in the form of certain specified flat and percentage fees paid to the partnership.

7. The offering memoranda issued to promote and sell each of the partnerships and to attract potential investors contained, among other things, the following:

a. A description of the transactions as outlined above;

b. A purportedly independent appraisal of the computer equipment, including an appraisal and valuation of its fair market value, residual value and useful life;

c. A purportedly independent appraisal of the master tape, including an appraisal and valuation of its fair market value and useful life, and a description of potential markets and licensees for the master tape; and

d. A tax opinion letter by defendant Lampf describing the tax benefits to be derived from investing in the partnership, including eligibility for an investment tax credit for the master tape transaction, depreciation of both equipment and master tape, and for investor interest expense, and partnership trade or business expenses and losses.

8. In or around April and/or October 1984, in connection with the settlement of litigation against them relating to

the limited partnerships known as Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum Associates, the packager defendants and defendant Lampf arranged to have all documents and materials relating to or generated in that litigation kept confidential and/or sealed by the court.

DESCRIPTION OF THE PLAINTIFFS

9. As more particularly described herein, plaintiffs are 49 individuals or entities that invested in one or more of the limited partnerships described herein.

DESCRIPTION OF THE DEFENDANTS

The Packagers

10. Defendants Leasing Consultants Associates ("LCA"), Leasing Consultants, Inc. ("LCI"), William L. McKenna ("McKenna"), Richard A. Heitmeyer ("Heitmeyer"), Richard D. Wellbrock ("Wellbrock") and William B. Ward ("Ward") acted as packagers and promoters of the tax shelter programs sold to plaintiffs, and conceived and arranged for the sale, purchase and lease transactions involved, procured the services of Lampf and other defendants, caused the preparation and dissemination of a model offering memorandum, solicited and procured broker/dealers and others to place or sell the limited partnership interests to plaintiffs, and solicited and procured appraisals for the equipment and master tapes.

11. Defendant LCA was at all relevant times a New Jersey general partnership comprised of defendants McKenna, Heitmeyer and Wellbrock.

12. Defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey, and was an affiliate of defendant LCA. Defendants McKenna, Heitmeyer, Wellbrock and Ward were officers

and controlling persons of LCI and were, at all relevant times, citizens of the state of New Jersey.

The Immediate Sellers

13. As described above, defendant LCA was at all relevant times a New Jersey general partnership.

14. As described above, defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey.

15. Defendant American Computer Equipment Leasing, Inc. ("ACE") was at all relevant times a corporation doing business in the state of New York.

16. Defendant Computer Systems Consultants, Inc. ("CSC") was at all relevant times a Delaware corporation with its principal office in Ridgewood, New Jersey.

The Equipment Sellers/Lessees

17. Defendant Analysis International Co., Inc. ("Analysis") is or was a corporation with its principal place of business in Charlotte, North Carolina. Defendant Anico Computer Leasing, Inc. ("Anico") is or was a North Carolina corporation and the parent corporation and controlling person of defendant Analysis. Defendants Amato Hernandez ("Hernandez") and John Chandler ("Chandler") are or were officers and controlling persons of Analysis and Anico.

18. Defendant Alanthus Computer Corporation ("Alanthus Computer") and defendant Alanthus Corporation ("Alanthus") are or were Delaware corporations. On information and belief, Alanthus Computer and/or Alanthus are now known as Technology Finance Group. On information and belief, Alanthus Computer and/or Alanthus may have been affiliated with Analysis International Co., Inc.

18a. Defendant Comdisco, Inc. ("Comdisco") is or was a corporation doing business in the state of Illinois, and

defendant Kenneth Pontikes ("Pontikes") is or was an officer and controlling person of Comdisco.

The Master Tape Lessees and Affiliates

19. Defendants Kirby Microprocessors, Inc. ("KMI") and Kirby Computer Systems, Inc. ("Kirby Computer") were at all relevant times corporations doing business in the state of New Jersey. Defendant Robert. M. Kirby ("Kirby") is or was the owner and controlling person of KMI and Kirby Computer.

20. Defendants Gordon S. Rosen Associates, Inc. ("Rosen Associates") and Software Systems for Word Processors, Inc. ("SSWPI") were at all relevant times corporations doing business in the state of New York. Defendant Gordon S. Rosen ("Rosen") is or was the owner and controlling person of Rosen Associates and SSWPI.

21. Defendants Robrech Systems, Inc. ("Robrech") and Digitize, Inc. ("Digitize") were all relevant times corporations doing business in the state of New York.

22. Defendants Buhler Software Services ("Buhler Software") and P-STAT, Inc. ("P-Stat") were at all relevant times corporations doing business in the state of New Jersey. Defendant Roald Buhler ("Buhler") is or was the owner and controlling person of Buhler Software and P-Stat.

23. Defendants ASG Program Products, Inc. ("ASG") and Applications Systems Group, Inc. ("Applications") were at all relevant times corporations doing business in the state of New York. Defendant Martin D. Pine ("Pine") is or was the president and/or controlling person of ASG and Applications.

23a. Defendant Mark Hanson was at all relevant times the president and controlling person of two entities known as Prose, Inc. and M.A. Hanson & Associates which were

a corporation and entity doing business in the state of Pennsylvania.

The Equipment Appraisers

24. Defendant Computer Value Associates ("Computer Value") was at all relevant times a company doing business in the state of New York. Defendant James Cuthbert ("Cuthbert") is or was the president and controlling person of Computer Value.

25. Defendants Texcom Equipment Corporation ("Texcom") and Global Computer Corporation ("Global") were at all relevant times corporations doing business in the state of Texas. Defendant Ronald Johnson ("Johnson") is or was the president, owner, and controlling person of Texcom and Global.

26. Defendant Berlent Industries, Inc. ("Berlent Industries") was at all relevant times a corporation doing business in the state of New York. Defendant Harvey N. Berlent ("Berlent") is or was the president and controlling person of Berlent Industries.

The Master Tape Appraisers

27. Defendant Ward was at all relevant times a citizen of the state of New Jersey.

28. Defendant ConServ International, Inc. ("ConServ") was at all relevant times a corporation doing business in the state of New Jersey. Defendant Robert W. Steinberger ("Steinberger") is or was the president and controlling person of ConServ. Prior to his association with ConServ, Steinberger was vice president of defendant Kirby Computer.

29. Defendant Technical Marketing Services, Inc. ("TMS") was at all relevant times a corporation doing business in the states of New York and New Jersey.

Defendant Leonard F. Turi ("Turi") is or was the president and controlling person of TMS.

29a. Defendant Edward Fizell was at all relevant times a citizen of the state of New Jersey.

The Attorneys

30. Defendant Lampf, Pleva, Lipkind, Prupis & Petigrow, P.C. ("Lampf") was at all relevant times a professional legal corporation with its principal place of business in the state of New Jersey. Lampf is now known as Lampf, Lipkind, Prupis & Petigrow, P.C.

Non-Defendant Co-Conspirators

31. The Lawrence Group was at all material times a consulting firm controlled by defendant William Ward. After the sales of the limited partnership units described herein, the Lawrence Group was engaged by the partnerships, at the suggestion of the packager defendants, purportedly to monitor the status of each of the partnerships' equipment and master tape leases and to make periodic reports to the partnerships describing this status.

FIRST CLAIM FOR RELIEF - DUVAL ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Duval plaintiffs.

32. The Duval plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

33. The following plaintiffs invested in the Duval Associates limited partnership in the amount and on the date indicated below. They shall be referred to herein as the "Duval plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Jack E. Evans	October 1979	$42,907

Earl D. Riddle	October 1979	42,907
Howard E. White	December 1979	28,604
Judith MacDonald	October 1979	28,604
Charles W. Botsford	October 1979	28,604
Jerry E. Marks	November 5, 1979	42,907
Theodore and Carolyn Beecher	October 1979	28,604
John V. Reitz	October 1979	28,604
Joseph C. Player	October 1979	28,604
Paul Winklesky	October 1979	14,302

34. The following defendants participated in the Duval Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Duval defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Duval partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Duval Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Duval defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendants Lampf to: act as general or special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Duval offering memorandum was

based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements, on which the Duval partnership agreement and sales and leases agreements were based; and

(7) Instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant CSC was the immediate seller for the Duval partnership. As described in paragraph 6a above, in this capacity, CSC was the entity which purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Duval equipment") purportedly consisted of an IBM 370/158 Central Processing Unit ("CPU"), an IBM 370/148 CPU, two IBM 370/138 CPU's, and approximately ten pieces of IBM peripheral equipment. The Duval partnership was to pay a total of $1,726,750 for this equipment. The master tape was of a software program known as Kirby Integrated Business Systems ("KIBS"), which was purportedly specially designed for use by home heating oil dealers and readily marketable within that industry. The Duval partnership was to pay a total of $2 million for this master tape. CSC played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that, by purchasing the Duval equipment and the KIBS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Duval partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. CSC was or should have been aware of its integral role in the Duval offering and of the lack of economic substance in these transactions in

that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. CSC knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Alanthus Computer was the equipment seller/lessee for the Duval partnership. As described in paragraph 6a above, in this capacity, Alanthus Computer was the entity which sold the Duval equipment to the immediate seller, CSC, for resale to the Duval partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the Duval equipment to the end users, which were represented to be General Motors, the Stop & Shop Companies, General Automation Company, and Hills-McCanna Company, and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Alanthus Computer played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that, by selling the Duval equipment to CSC for resale to the Duval partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that CSC had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Alanthus Computer also added credence to the reasonableness of the end-user lease terms described in the Duval offering memorandum, and thus helped to

substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Alanthus Computer also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Alanthus Computer was or should have been aware of its integral role in the Duval offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Alanthus Computer knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life, and residual value of the equipment.

d. Defendant Kirby Computer was the master tape lessee for the Duval partnership. As described in paragraph 6b above, in this capacity, Kirby Computer was the entity that leased the KIBS master tape back from the Duval partnership and was to market and obtain licensees for the use of the master tape. Defendant KMI was an affiliate of Kirby Computer and was the master tape seller for the Duval partnership. As described in paragraph 6b above, in this capacity, KMI was the entity that sold the KIBS master tape to CSC, the immediate seller, for resale to the Duval partnership. Defendant Kirby was the owner and controlling person of KMI and Kirby Computer. KMI, Kirby Computer, and/or Kirby had purportedly developed the KIBS software program and had purported expertise in marketing the KIBS master tape. On information and belief, Kirby formed Kirby Computer and/or KMI solely

for purposes of participating in the Duval partnership. KMI and Kirby played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that, by selling the KIBS master tape to CSC for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if CSC had purchased the tape from an independent third party in an arm's length, negotiated transaction. Kirby Computer and Kirby played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that, by virtue of their purported expertise in the KIBS software program and in the marketing of this software, they appeared capable of successfully exploiting the KIBS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. KMI, Kirby Computer, and Kirby were or should have been aware of their integral role in the Duval offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the KIBS master tape would be used by the packagers in a limited partnership offering. KMI, Kirby Computer, and Kirby knew or should have known that the KIBS master tape transactions described herein would be used to induce the investors to invest in the partnership, and that investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the KIBS master tape.

e. Defendant Berlent Industries was the equipment appraiser for the Duval partnership. Defendant Berlent was the president and controlling person of Berlent Industries. Defendants Berlent Industries and Berlent prepared a written appraisal of the Duval equipment, on or about October 19, 1979 (hereinafter the "Berlent-Duval ap-

praisal"), which appeared in the Duval offering memorandum, and which represented that the fair market value of the Duval equipment was $1.552 million, that the equipment had a useful life in excess of nine years, and that at the end of the nine-year period, its fair market value would be $310,000. Berlent Industries and Berlent played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that the Berlent-Duval appraisal justified the inflated price the partnership was to pay for the Duval equipment and provided the limited partners with "independent" substantiation for the assumptions in the Duval offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value after the expiration of the end-user leases from which the partnership would derive bonus rentals. Berlent Industries and Berlent were or should have been aware that the Berlent-Duval appraisal would be disseminated to prospective investors in Duval Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Berlent-Duval appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Duval equipment.

f. In addition to his role as a packager, defendant Ward was also the master tape appraiser for the Duval partnership. In this capacity, he prepared a written appraisal of the KIBS master tape, on or about August 30, 1979 (hereinafter the "Ward-Duval appraisal"), which appeared in the Duval offering memorandum, and which represented that the fair market value of the KIBS master tape to be purchased from KMI and leased to Kirby Computer was in excess of $2 million, and that it had a useful life in excess of seven years. This appraisal also represented that representatives of the Data General Corporation would be actively engaged in marketing the KIBS master tape. This appraisal also represented that the purchase price that the Duval partnership was paying for the KIBS master tape was equal or close to its appraised fair market value. This appraisal also represented that defendant Ward had met with the management of Kirby Computer and KMI and had reviewed in detail the operation of the KIBS master tape. Ward played an integral and essential role in the fraud perpetrated upon the Duval plaintiffs in that the Ward-Duval appraisal justified the inflated price the partnership was to pay for the KIBS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Duval offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the KIBS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least seven years. Ward was or should have been aware that the Ward-Duval appraisal would be disseminated to prospective investors in Duval Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Ward-Duval appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the KIBS master tape.

g. Defendant Lampf was the general or special tax counsel for the Duval partnership. In this capacity, Lampf issued a special written tax opinion for the Duval partnership, in or about October 1979 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Duval offering memorandum, and upon which it knew potential investors, including the Duval plaintiffs, would rely in making their investment in Duval Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Duval Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least

$20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Duval offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Duval partnership agreement and sale lease agreements were based.

35. Beginning in or around September 1979, and continuing to the present, the Duval defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Duval plaintiffs in connection with the sale of limited partnership interests in Duval Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Duval computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Duval investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

36. The Duval plaintiffs were induced to invest in Duval Associates by means of an offering memorandum dated September 10, 1979, and a supplemental offering memorandum dated October 26, 1979 (hereinafter collectively "the Duval offering memorandum"), which included the Lampf tax opinion, the Berlent-Duval appraisal, and the Ward-Duval appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 34b above, the end users that were purportedly already leasing this equipment, as described in paragraph 34c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 34b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 34e and f above, and the tax benefits

and profits to be derived from investing in the partnership, as described in paragraph 7d above.

37. The Duval offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Duval partnership had been, or would be, involved.

38. In connection with the sale of interests in Duval Associates to the Duval plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated from licensing KIBS master tape and from the lease income and residual value in the Duval equipment.

b. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws.

c. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that the KIBS master tape program was ready to be marketed in its then-existing format and would readily achieve a significant market share in its target market.

d. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the KIBS master tape program was tangible, new, original, and previously unexploited property, and therefore qualified for investment tax credit.

e. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that Kirby Computer and KMI, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the KIBS master tape and thereby generate revenues for the Duval partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership.

f. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that Ward had met with the management of Kirby Computer and KMI and had become familiar with the operation of the KIBS program.

g. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Berlent Industries and Berlent, in the Berlent-Duval appraisal, represented that the fair market value, residual value, and useful life attributed to the Duval equipment were reasonable and accurate.

h. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that the fair market value and useful life attributed to the KIBS master tape were reasonable and accurate.

i. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the parties involved in the Duval sale and lease transactions had no conflicts of interest not disclosed in the Duval offering memorandum.

39. These representations were false and misleading in that:

a. The profits promised in the Duval offering memorandum and in the Lampf tax opinion could not be realized by the Duval plaintiffs.

b. The actual fair market value, residual value, and useful life of the Duval equipment were substantially less than represented.

c. The actual fair market value and useful life of the KIBS master tape were substantially less than represented.

d. The KIBS master tape was not readily marketable in its target market without substantial modifications in format.

e. On information and belief, the KIBS master tape program was not tangible, new, original, or previously unexploited properly, and therefore not qualified for investment tax credit.

f. KMI and Kirby Computer did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the KIBS master tape.

g. On information and belief, before issuing the Ward-Duval appraisal, Ward had not met with the management of Kirby Computer and KMI, and had not tested or run the KIBS program and was not familiar with its operation.

h. Ward was a principal of defendant LCI, and therefore had conflicts of interest not disclosed in the Duval offering memorandum.

40. In making the representations described above, the following Duval defendants failed to disclose the following material facts to the Duval plaintiffs:

a. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the actual fair market value, residual value, and useful life of the Duval equipment were substantially less than represented in the Duval offering memorandum and in the Berlent-Duval appraisal;

b. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the Duval equipment was already or would likely become obsolete shortly after it was purchased by the Duval partnership in that IBM had announced the introduction of new, better systems that would render the Duval equipment obsolete;

c. The packagers, Lampf, and Ward failed to disclose that the actual fair market value and useful life of the KIBS master tape were substantially less than represented in the Duval offering memorandum and in the Ward-Duval appraisal;

d. The packagers, Lampf, and Ward failed to disclose that the Ward-Duval appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

e. The packagers, Lampf, and Ward failed to disclose that before issuing the Ward-Duval appraisal, Ward had not met with the management of Kirby Computer and KMI, had not tested or run the KIBS program and was not familiar with its contents and operation, and had not adequately researched the marketability of the KIBS master tape;

f. The packagers, Lampf, and Ward failed to disclose that the KIBS master tape was not readily marketable in its target market without substantial modifications in format;

g. The packagers, Lampf, and Ward, failed to disclose that, in order to achieve the market share projected in the Ward-Duval appraisal, the expenses of marketing the KIBS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

h. The packagers and Lampf failed to disclose that Ward was a principal in defendant LCI, and therefore had

conflicts of interest not disclosed in the Duval offering memorandum;

i. The packagers, Lampf, and Ward failed to disclose that Kirby Computer and KMI were undercapitalized and without sufficient skill, expertise, and personnel to market and license the KIBS master tape and generate revenues for the partnership; and

j. The packagers, Lampf, CSC, Alanthus Computer, Berlent Industries, and Berlent failed to disclose that the Duval plaintiffs would not and could not obtain title to the Duval equipment because of the terms and nature of a preexisting transaction involving the Duval equipment.

41. Defendants Berlent, Berlent Industries, Ward, CSC, Alanthus Computer, KMI, Kirby Computer, and Kirby aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Duval partnership and their actions in furtherance of these roles, as described in paragraphs 34b-f above, were essential components of the fraud perpetrated on the Duval plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Duval plaintiffs.

42. Beginning in and around September 1979, and continuing until the present, the Duval defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around February 1980, the packager defendants arranged for The Lawrence Group to be engaged to act as consultant to the partnership and continually assured and represented to the Duval plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Duval equipment lease were current and that diligent efforts were being made to market and obtain licensees for the KIBS master tape when, in fact, equipment lease payments owed to the partnership were

sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

43. The Duval plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Duval defendants, as described herein. The Duval plaintiffs had no reason to believe that the Duval defendants omitted to state material facts, as described herein. The Duval plaintiffs were not aware of the true facts or the facts that the Duval defendants omitted to state. The Duval plaintiffs were entitled to and did rely on the Duval defendants' representations, as described herein, and would not have purchased any interests in the Duval limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

44. The Duval plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

45. The Duval plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Duval plaintiffs and concealed the fraud alleged herein by means of the affirmative acts described in paragraph 8 and 42 above. If the Duval plaintiffs or their agents knew of any facts potentially giving rise to the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 42 above, led them, under the circumstances described herein,

to disregard those facts and to reasonably believe that they did not have a claim for relief.

46. The Duval plaintiffs hereby tender their limited partnership interests to the Duval defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b))

53. The Duval plaintiffs reallege and incorporate by reference paragraphs 1-46 above.

54. In connection with the sale of limited partnership interests in Duval Associates, defendants LCA, LCI, McKenna, Wellbrock, Heitmeyer, Ward, and Lampf (the "Duval primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Duval plaintiffs, made untrue statements of material fact, as described in paragraphs 38-39 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 40 above, and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Duval plaintiffs.

55. The Duval primary violators, and each of them, knew of the falsity of the representations described in paragraph 38 above, or recklessly failed to ascertain the truth of the representations. The Duval primary violators knew of the omissions of material fact described in paragraph 40 above, or recklessly failed to disclose these facts.

56. Defendants CSC, Alanthus Computer, Berlent, Berlent Industries, Ward, KMI, Kirby, and Kirby Computer (the "Duval aiders and abettors") knew that their actions,

as described in paragraphs 34b-f and 41 above, furthered and provided substantial assistance to the Duval primary violators in committing a fraud on the Duval plaintiffs.

57. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

58. As a result of these acts, the Duval plaintiffs are entitled to recover damages equal to all sums paid for their investments, together with interest thereon since the date paid.

* * *

SECOND CLAIM FOR RELIEF - LaMAR ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the LaMar plaintiffs.

106. The LaMar plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

107. The following plaintiffs invested in the LaMar Associates limited partnership in the amount and on the date indicated below. They shall be referred to herein as the "LaMar plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Dale R. Peterson	12/25/79	$31,971
Harlan C. Selby	12/20/79	31,971

108. The following defendants participated in the LaMar partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "LaMar defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the LaMar partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed LaMar Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other LaMar defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendant Lampf to: act as general or special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the LaMar offering memorandum was based, and prepare, print and distribute a model partnership agreement and model sales and lease agreements on which the LaMar partnership agreement and sales and lease agreements were based; and

(7) Instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant CSC was the immediate seller for the LaMar partnership. As described in paragraph 6a above, in this capacity, CSC was the entity which purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "LaMar equipment") purportedly consisted of an IBM 370/168 CPU and approximately seven pieces of IBM peripheral equipment. The LaMar partner-

ship was to pay a total of $1,726,750 for this equipment. The master tape was of a software program known as Automated Information Display System ("AID"), which was purportedly specially designed for use by emergency response organizations, such as police and fire departments, and was purportedly readily marketable to such organizations. The LaMar partnership was to pay a total of $2.45 million for this master tape. CSC played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that, by purchasing the LaMar equipment and the AID master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the LaMar partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. CSC was or should have been aware of its integral role in the LaMar offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. CSC knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Alanthus was the equipment seller/lessee for the LaMar partnership. As described in paragraph 6a above, in this capacity, Alanthus was the entity that sold

the IBM equipment to the immediate seller, CSC, for resale to the LaMar partnership, and then leased the equipment back from the partnership. Alanthus was also the entity that had, purportedly, previously leased the equipment to the end user, which was represented to be Associated Hospital Service, Inc., an affiliate of Blue Cross of Wisconsin, and was to re-lease the equipment to a subsequent end user when the existing user lease expired. Alanthus played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that, by selling the LaMar equipment to CSC for resale to the LaMar partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that CSC had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Alanthus also added credence to the reasonableness of the end-user lease terms described in the LaMar offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Alanthus also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user lease, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Alanthus was or should have been aware of its integral role in the LaMar offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Alanthus knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on

the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life, and residual value of the equipment.

d. Defendant Digitize was the master tape lessee for the LaMar partnership. As described in paragraph 6b above, in this capacity, Digitize was the entity that leased the AID master tape back from the LaMar partnership and was to market and obtain licensees for the use of the master tape. Defendant Robrech was an affiliate of Digitize and was the master tape seller for the LaMar partnership. As described in paragraph 6b above, in this capacity, Robrech was the entity that sold the AID master tape to CSC, the immediate seller, for resale to the LaMar partnership. Digitize and/or Robrech had purportedly developed the AID software program and had purported expertise in marketing the AID master tape. On information and belief, Digitize and/or Robrech were formed solely for purposes of participating in the LaMar partnership. Robrech played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that, by selling the AID master tape to CSC for resale to the partnership, it made the purchase price of the tape appear reasonable by making it appear as if CSC had purchased the tape from an independent third party in an arm's length, negotiated transaction. Digitize played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that, by virtue of its purported expertise in the AID software program and in the marketing of this software, it appeared capable of successfully exploiting the AID master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Robrech and Digitize were or should have been aware of their integral role in the LaMar offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the AID master tape would be used by the packagers in a limited partnership offering. Robrech and Digitize knew or should have known that the AID master tape transactions described herein would be used to induce the investors to invest in the partnership, and that investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the AID master tape.

e. Defendant Berlent Industries was the equipment appraiser for the LaMar partnership. Defendant Berlent was the president and controlling person of Berlent Industries. Defendant Berlent Industries and Berlent prepared a written appraisal of the LaMar equipment, on or about November 6, 1979 (hereinafter "the Berlent-LaMar appraisal"), which appeared in the LaMar offering memorandum, and which represented that the current fair market value for the LaMar equipment was $1.85 million, that it had a useful life in excess of nine years, and that at the end of nine years, it would have a residual value of $420,000. Berlent Industries and Berlent played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that the Berlent-LaMar appraisal justified the inflated price the partnership was to pay for the LaMar equipment and provided the limited partners with "independent" substantiation for the assumptions in the LaMar offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end-user lease, from which the partnership would derive bonus rentals. Berlent Industries and Berlent were or should have been aware that the Berlent-LaMar appraisal would be disseminated to prospective investors in LaMar Associates and would be used to induce these investors to invest in the partnership, and that these investors

would rely upon the Berlent-LaMar appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the LaMar equipment.

f. In addition to his role as a packager, defendant Ward was also the master tape appraiser for the LaMar partnership. In this capacity, he prepared a written appraisal of the AID master tape, on or about November 26, 1979 (hereinafter "the Ward-LaMar appraisal"), which appeared in the LaMar offering memorandum, and which represented that the fair market value of the AID master tape to be purchased from Robrech and leased to Digitize was in excess of $2.5 million, and that its useful life was at least seven years. This appraisal also represented that the purchase price that the LaMar partnership was paying for the AID master tape was equal or close to this appraisal fair market value. This appraisal also represented that defendant Ward had met with the management, sales, and technical staff of Robrech and Digitize, had reviewed in detail the contents of the AID master tape, and had conducted independent market research into the target market for the KIBS master tape. Ward played an integral and essential role in the fraud perpetrated upon the LaMar plaintiffs in that the Ward-LaMar appraisal justified the inflated price the partnership was to pay for the AID master tape and provided the limited partners with "independent" substantiation for the assumptions in the LaMar offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the AID master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least seven years. Ward was or should have been aware that the Ward-LaMar appraisal would be disseminated to prospective investors in LaMar Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Ward-LaMar appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the AID master tape.

g. Defendant Lampf was the general or special tax counsel for the LaMar partnership. In this capacity, Lampf issued a special written tax opinion for the LaMar partnership, in or about December 1979 (hereinafter "the Lampf tax opinion"), which it knew would appear in the LaMar offering memorandum, and upon which it knew potential investors, including the LaMar plaintiffs, would rely in making their investments in LaMar Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in LaMar Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the LaMar offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the LaMar partnership agreement and sales and lease agreements were based.

109. Beginning in or around November 1979, and continuing to the present, the LaMar defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the LaMar plaintiffs in connection with the sale of limited partnership interests in LaMar Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the LaMar computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the LaMar investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

110. The LaMar plaintiffs were induced to invest in LaMar Associates by means of an offering memorandum

dated November 30, 1979 (hereinafter "the LaMar offering memorandum"), which included the Lampf tax opinion, the Berlent-LaMar appraisal, and the Ward-LaMar appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 108b above, the end user that was purportedly already leasing this equipment, as described in paragraph 108c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 108b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 108e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above.

111. In connection with the sale of interests in LaMar Associates to the LaMar plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated from licensing the AID master tape and from the lease income and residual value in the LaMar equipment.

b. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws.

c. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that the AID master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market.

d. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the AID master tape program was tangible, new, original, and previously unexploited property, and therefore qualified for investment tax credit.

e. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that Digitize and Robrech, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the AID master tape and thereby generate revenues for the LaMar partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership.

f. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that Ward had met with the management and staff of Robrech and Digitize, had become familiar with the contents of the AID program, and had conducted independent research into the marketability of the AID master tape.

g. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Berlent Industries and Berlent, in the Berlent-LaMar appraisal, represented that the residual value and useful life attributed to the LaMar equipment were reasonable and accurate.

h. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that the fair market value and useful life attributed to the AID master tape were reasonable and accurate.

i. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the parties involved in the LaMar sale and lease trans-

actions had no conflicts of interest not disclosed in the LaMar offering memorandum.

112. These representations were false and misleading in that:

a. The profits promised in the LaMar offering memorandum and in the Lampf tax opinion could not be realized by the LaMar plaintiffs.

b. The actual residual value and useful life of the LaMar equipment were substantially less than represented.

c. The actual fair market value and useful life of the AID master tape were substantially less than represented.

d. The AID master tape was not readily marketable in its target market without substantial modifications in format.

e. On information and belief, the AID master tape program was not tangible, new, original, or previously unexploited property, and therefore not qualified for investment tax credit.

f. Robrech and Digitize did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the AID master tape.

g. On information and belief, before issuing the Ward-LaMar appraisal, Ward had not met with the management and staff of Robrech and Digitize, had not tested or run the AID program and was not familiar with its contents and operation, and had not independently or thoroughly researched the marketability of the AID master tape.

h. Ward was a principal in defendant LCI, and therefore had conflicts of interest not disclosed in the LaMar offering memorandum.

113. In making the representations described above, the following LaMar defendants failed to disclose the following material facts to the LaMar plaintiffs:

a. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the actual residual value and useful life of the LaMar equipment were substantially less than represented in the LaMar offering memorandum and in the Berlent-LaMar appraisal;

b. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the LaMar equipment was already or would likely become obsolete shortly after it was purchased by the LaMar partnership in that IBM had announced the introduction of new, better systems that would render the LaMar equipment obsolete;

c. The packagers, Lampf, and Ward failed to disclose that the actual fair market value and useful life of the AID master tape program were substantially less than represented in the LaMar offering memorandum and in the Ward-LaMar appraisal;

d. The packagers, Lampf, and Ward failed to disclose that the Ward appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

e. The packagers, Lampf, and Ward failed to disclose that before issuing the Ward-LaMar appraisal, Ward had not met with the management and staff of Robrech and Digitize, had not tested or run the AID program and was not familiar with its contents and operation, and had not independently or adequately researched the marketability of the AID master tape;

f. The packagers, Lampf, and Ward failed to disclose that, in order to achieve the market share projected in the Ward-LaMar appraisal, the expenses of marketing the AID master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

g. The packagers and Lampf failed to disclose that Ward was a principal in defendant LCI and therefore had conflicts of interest not disclosed in the LaMar offering memorandum;

h. The packagers, Lampf, and Ward failed to disclose that Robrech and Digitize were undercapitalized and without sufficient skill, expertise, and personnel to market and license the AID master tape and generate revenues for the partnership;

i. The packagers, Lampf, and Ward failed to disclose that the AID master tape was not readily marketable in its target market without substantial modifications in format; and

j. The packagers, Lampf, CSC, Alanthus Computer, Berlent Industries, and Berlent failed to disclose that the LaMar plaintiffs would not and could not obtain title to the LaMar equipment because of the terms and nature of a preexisting transaction involving the LaMar equipment.

114. Defendants Berlent, Berlent Industries, Ward, CSC, Alanthus, Robrech, and Digitize aided and abetted in the misrepresentations and omissions alleged above in that their roles in the LaMar partnership and their actions in furtherance of these roles, as described in paragraphs 108b-f above, were essential components of the fraud perpetrated on the LaMar plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the LaMar plaintiffs.

115. Beginning in and around November 1979, and continuing until the present, the LaMar defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around April 1980, the packager defendants arranged for The Lawrence Group to be engaged to act as consultant to the partnership and continually assured and represented to the LaMar plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the LaMar equipment lease were current and that diligent efforts were being made to market and obtain licensees for the AID master tape when, in fact, equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

116. The LaMar plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the LaMar defendants, as described herein. The LaMar plaintiffs had no reason to believe that the LaMar defendants omitted to state material facts, as described herein. The LaMar plaintiffs were not aware of the true facts or the facts that the LaMar defendants omitted to state. The LaMar plaintiffs were entitled to and did rely on the LaMar defendants' representations, as described herein, and would not have purchased any interests in the LaMar limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

117. The LaMar plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

118. The LaMar plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did

mislead the LaMar plaintiffs and concealed the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 115 above. If the LaMar plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 115 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

119. The LaMar plaintiffs hereby tender their limited partnership interests to the LaMar defendants.

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COUNT II

(1934 Securities Exchange Act - Section 10(b))

126. The LaMar plaintiffs reallege and incorporate by reference paragraphs 1-31 and 107-119 above.

127. In connection with the sale of the limited partnership interests in LaMar Associates, defendants LCA, LCI, McKenna, Wellbrock, Heitmeyer, Ward, and Lampf (the "LaMar primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the LaMar plaintiffs, made untrue statements of material fact, as described in paragraphs 111-112 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading as described in paragraph 113 above, and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the LaMar plaintiffs.

128. The LaMar primary violators, and each of them, knew of the falsity of the representations described in paragraph 111 above, or recklessly failed to ascertain the

truth of the representations. The LaMar primary violators knew of the omissions of material fact described in paragraph 113 above, or recklessly failed to disclose these fact.

129. Defendants CSC, Alanthus, Berlent, Berlent Industries, Ward, Robrech, and Digitize (the "LaMar aiders and abettors") knew that their actions, as described in paragraphs 108b-f and 114 above, furthered and provided substantial assistance to the LaMar primary violators in committing a fraud on the LaMar plaintiffs.

130. These defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

131. As a result of these acts, the LaMar plaintiffs are entitled to recover damages equal to all sums paid for their investments, together with interest thereon since the date paid.

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THIRD CLAIM FOR RELIEF - MT. HOOD ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Mt. Hood plaintiffs.

187. The Mt. Hood plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

188. The following plaintiffs invested in the Mt. Hood Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Mt. Hood plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Dale R. Peterson	9/16/80	$61,610
Earl D. Riddle	9/18/80	30,805
Harlan C. Selby	9/17/80	30,805
Nickolas J. Madesh	9/23/80	30,805
Robert A. Graham	9/17/80	30,805
Jerry E. Marks	9/22/80	30,805
Clifford B. Alterman	9/19/80	30,805
Ruth Beecher	9/15/80	30,805
Howard H. Overback	9/23/80	30,805
John v. Reitz	9/23/80	30,805
Theodore and Edith Trykar	9/15/80	30,805
Floyd E. Hambleton	9/12/80	30,805
Ward E. Moore	9/80	30,805

189. The following defendants participated in the Mt. Hood Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Mt. Hood defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Mt. Hood partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Mt. Hood Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Mt. Hood defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Mt. Hood offering memorandum was based and prepare, print, and distribute a model partnership agreement and model sales and lease agreements on which the Mt. Hood partnership agreement and sales and lease agreements were based; and

(7) Instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant ACE was the immediate seller for the Mt. Hood partnership. As described in paragraph 6a above, in this capacity, ACE was the entity which purchased the IBM equipment and the master tape from the equipment seller and master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Mt. Hood equipment") purportedly consisted of an IBM 370/158 CPU and approximately 26 pieces of IBM peripheral equipment. The Mt. Hood partnership was to pay a total of $1.75 million for this equipment. The master tape was of a software program known as the P-Stat Preprocessor Program ("P-STAT"), which was purportedly specially designed to allow computer programs written in the Fortran language to be economically adapted for use on most makes of computers, and was purportedly readily marketable for that function to major companies and other businesses using several different makes of computers. The Mt. Hood partnership was to pay a total of $2.3 million for this master tape. ACE played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by purchasing the Mt. Hood equipment and P-STAT master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Mt. Hood partnership, it obscured the original purchase price of the equipment and

master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. ACE was or should have been aware of its integral role in the Mt. Hood offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. ACE knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Analysis was the equipment seller/lessee for the Mt. Hood Associates partnership. As described in paragraph 6a above, in this capacity, Analysis was the entity that sold the IBM equipment to the immediate seller, ACE, for resale to the Mt. Hood partnership, and then leased the equipment back from the partnership. Analysis was also the entity that had, purportedly, previously leased the Mt. Hood equipment to the end user, which was represented to be the Russell Corporation, and was to release the equipment to a subsequent end user when the existing user lease expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by selling the Mt. Hood equipment to ACE for resale to the Mt. Hood partnership, it further

obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that ACE had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end-user lease terms described in the Mt. Hood offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user lease, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnerhip had to seek its own lessees. Analysis was or should have been aware of its integral role in the Mt. Hood offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Analysis knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life, and residual value of the equipment.

d. Defendant P-Stat was the master tape lessee for the Mt. Hood partnership. As described in paragraph 6b above, in this capacity, P-Stat was the entity that leased the P-STAT master tape back from the Mt. Hood partnership and was to market and obtain licensees for the use of the master tape. Defendant P-Stat was an affiliate of Buhler Software, which was the master tape seller for the Mt. Hood partnership. As described in paragraph 6b

above, in this capacity, Buhler Software was the entity that sold the P-STAT master tape to ACE, the immediate seller, for resale to the Mt. Hood partnership. Defendant Buhler was the owner and controlling person of Buhler Software and P-Stat. Buhler Software, P-Stat and/or Buhler had purportedly developed the P-Stat software program and had purported expertise in marketing the P-STAT master tape. On information and belief, Buhler formed Buhler Software and/or P-Stat solely for purposes of participating in the Mt. Hood partnership. Buhler Software and Buhler played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by selling the P-STAT master tape to ACE for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if ACE had purchased the tape from an independent third party in an arm's length, negotiated transaction. P-Stat and Buhler played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by virtue of their purported expertise in the P-Stat software program and in the marketing of this software, they appeared capable of successfully exploiting the P-STAT master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Buhler Software, P-Stat, and Buhler were or should have been aware of their integral role in the Mt. Hood offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the P-STAT master tape would be used by the packagers in a limited partnership offering. Buhler Software, P-Stat, and Buhler knew or should have known that the P-STAT master tape transactions described herein would be used to induce the investors to invest in the partnership, and that investors would rely

on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the P-STAT master tape.

e. Defendant Texcom was the equipment appraiser for the Mt. Hood partnership. Defendant Johnson was the president, owner, and controlling person of Texcom. Defendants Texcom and Johnson prepared a written appraisal of the Mt. Hood equipment, on or about July 31, 1980 (hereinafter "the TexCom appraisal"), which appeared in the Mt. Hood offering memorandum, and which represented that the Mt. Hood equipment had a fair market value of $1.8 million, had a useful life in excess of nine years, and would have a residual value at the end of nine years in excess of $360,000. Texcom and Johnson played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that the Texcom appraisal justified the inflated price the partnership was to pay for the Mt. Hood equipment and provided the limited partners with "independent" substantiation for the assumptions in the Mt. Hood offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end-user lease, from which the partnership would derive bonus rentals. Texcom and Johnson were or should have been aware that the Texcom appraisal would be disseminated to prospective investors in Mt. Hood Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Texcom appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Mt. Hood equipment.

f. Defendant ConServ was the master tape appraiser for the Mt. Hood partnership. Defendant Steinberger was the president and controlling person of ConServ.

Defendants ConServ and Steinberger prepared a written appraisal of the P-STAT master tape, on or about August 1, 1980 (hereinafter "the ConServ appraisal"), which appeared in the Mt. Hood offering memorandum, and which represented that the fair market value of the P-STAT master tape to be purchased from Buhler Software and leasd to P-Stat was in excess of $2.4 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Mt. Hood partnership was paying for the P-STAT master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Steinberger had met with the management and technical staff of Buhler Software and P-Stat, had examined in detail the contents of the P-STAT master tape, and had discussed with Buhler Software and P-STAT the underlying objective of the P-Stat program, its current development and operational status, and the market segment that could benefit from licensing the P-STAT master tape. ConServ and Steinberger played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that the ConServ appraisal justified the inflated price the partnership was to pay for the P-STAT master tape and provided the limited partners with "independent" substantiation for the assumptions in the Mt. Hood offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the P-STAT master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. ConServ and Steinberger were or should have been aware that the ConServ appraisal would be disseminated to prospective investors in Mt. Hood Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the ConServ appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the P-STAT master tape.

g. Defendant Lampf was the special tax counsel for the Mt. Hood partnership. In this capacity, Lampf issued a special written tax opinion for the Mt. Hood partnership, in or about October 1980 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Mt. Hood offering memorandum, and upon which it knew potential investors, including the Mt. Hood plaintiffs, would rely in making their investment in Mt. Hood Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Mt. Hood Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Mt. Hood offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Mt. Hood Associates partnership agreement and sales and lease agreements were based.

190. Beginning in or around August 1980, and continuing to the present, the Mt. Hood defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Mt. Hood plaintiffs in connection with the sale of limited partnership interests in Mt. Hood Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Mt. Hood computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Mt. Hood investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

191. The Mt. Hood plaintiffs were induced to invest in Mt. Hood Associates by means of an offering memorandum dated August 1, 1980 (hereinafter "the Mt. Hood offering

memorandum"), which included the Lampf tax opinion, the Texcom appraisal, and the ConServ appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 189b above, the end user that was purportedly already leasing this equipment, as described in paragraph 189c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 189b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 189e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Steinberger, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants in the Mt. Hood partnership had been, or would be, involved.

192. In connection with the sale of interests in Mt. Hood Associates to the Mt. Hood plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated from licensing the P-STAT master tape and from the lease income and residual value in the Mt. Hood equipment.

b. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement

to tax benefits and the legitimacy of the program under existing applicable laws.

c. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the Mt. Hood equipment existed, was specifically identified, and was already under lease to the Russell corporation on terms that would provide sufficient income to cover the lease payments to the seller.

d. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that the P-STAT master tape program was ready to market in its then-existing format and would readily achieve a significant market share in its target market.

e. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the P-STAT master tape progra n was tangible, new, original, and previously unexploited property, and therefore qualified for investment tax credit.

f. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that P-Stat and Buhler Software, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the P-STAT master tape and thereby generate revenues for the Mt. Hood partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership.

g. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that Steinberger had met with the management and staff of Buhler Software and P-STAT, and had become familiar

with the contents and operation of the P-Stat program and the marketing potential of the P-Stat master tape.

h. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and Texcom and Johnson, in the Texcom appraisal, represented that the fair market value, residual value, and useful life attributed to the Mt. Hood equipment were reasonable and accurate.

i. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that the fair market value and useful life attributed to the P-STAT master tape were reasonable and accurate.

193. These representations were false and misleading in that:

a. The IBM computer equipment described in the Mt. Hood offering memorandum did not exist or was not under lease to the end user, the Russell corporation, as represented.

b. The profits promised in the Mt. Hood offering memorandum and in the Lampf tax opinion could not be realized by the Mt. Hood plaintiffs.

c. The actual fair market value, residual value, and useful life of the Mt. Hood equipment were substantially less than represented.

d. The actual fair market value and useful life of the P-STAT master tape were substantially less than represented.

e. The P-STAT master tape was not readily marketable in its target market without substantial modifications in format.

f. On information and belief, the P-STAT master tape program was not tangible, new, original, or previously unexploited property, and therefore not qualified for investment tax credit.

g. Buhler Software and P-Stat, did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the P-STAT master tape.

h. On information and belief, before issuing the ConServ appraisal, Steinberger was not familiar with the P-Stat program contents and operation, and had not thoroughly investigated the marketability of the P-STAT master tape.

194. In making the representations described above, the following Mt. Hood defendants failed to disclose the following material facts to the Mt. Hood plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Mt. Hood offering memorandum was not in fact the equipment owned by ACE or Analysis and purchased by the partnership;

b. The packagers and Lampf failed to disclose that the IBM equipment described in the Mt. Hood offering memorandum was not currently under lease to the Russell Corporation, the purported end user;

c. The packagers, Lampf, Texcom, and Johnson failed to disclose that the actual fair market value, residual value, and useful life of the Mt. Hood equipment were substantially less than represented in the Mt. Hood offering memorandum and in the Texcom appraisal;

d. The packagers, Lampf, Texcom, and Johnson failed to disclose that they had not performed any investigation to examine the equipment or to verify its existence and condition;

e. The packagers, Lampf, Texcom, and Johnson failed to disclose that the Mt. Hood IBM equipment was essentially obsolete at the time it was purchased by the Mt. Hood partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the actual fair market value and useful life of the P-STAT master tape were substantially less than represented in the Mt. Hood offering memorandum and in the ConServ appraisal;

g. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the ConServ appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Lampf, ConServ, and Steinberger failed to disclose that before issuing the ConServ appraisal, Steinberger had not adequately investigated the marketability of the P-STAT master tape;

i. The packagers, Lampf, ConServ, and Steinberger failed to disclose that, in order to achieve the market share projected in the ConServ appraisal, the expenses of marketing the P-STAT master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

j. The packagers, Lampf, ConServ, and Steinberger failed to disclose that Buhler Software and P-Stat were undercapitalized and without sufficient skill, expertise, and personnel to market and license the P-STAT master tape and general revenues for the partnership;

k. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the P-STAT master tape was not readily marketable in its target market without substantial modifications in format; and

l. The packagers, Lampf, ACE, Analysis, Texcom, and Johnson failed to disclose that the Mt. Hood plaintiffs would not and could not obtain title to the Mt. Hood equipment because of the terms and nature of preexisting transactions involving the Mt. Hood equipment.

195. Defendants Johnson, Texcom, ConServ, Steinberger, ACE, Analysis, Hernandez, Chandler, Anico, Buhler Software, P-Stat, and Buhler aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Mt. Hood partnership and their actions in furtherance of these roles, as described in paragraphs 189b-f above, were essential components of the fraud perpetrated on the Mt. Hood plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Mt. Hood plaintiffs.

196. Beginning in and around August 1980, and continuing until the present, the Mt. Hood defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around February 1981, the packager defendants arranged for Mr. Steinberger to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Mt. Hood plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Mt. Hood equipment lease were current and that diligent efforts were being made to market and obtain licensees for the P-STAT master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

197. In or around August 1982, the Mt. Hood partnership sought to rescind its purchase of the P-STAT master tape because efforts to obtain licensees for the master tape had not been as successful as hoped. In or around October 1982, in connection with this rescission and in an effort to mislead the Mt. Hood limited partners and to conceal

the fraud alleged herein, the packagers and/or their attorney, Michael Dell, represented to and assured the attorneys for the Mt. Hood partnership, Burt & Hagen, P.C., that the marketing difficulties encountered by the master tape marketers were the result of unforeseen circumstances and that the packagers stood behind the representations in the Mt. Hood offering memorandum. In a further effort to lull the Mt. Hood limited partners and to conceal the fraud alleged herein, the packagers arranged for the seller of the P-STAT master tape to repurchase the tape at no loss to the partnership, and procured a substitute real estate investment for the partnership.

198. The Mt. Hood plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Mt. Hood defendants, as described herein. The Mt. Hood plaintiffs had no reason to believe that the Mt. Hood defendants omitted to state material facts, as described herein. The Mt. Hood plaintiffs were not aware of the true facts or the facts that the Mt. Hood defendants omitted to state. The Mt. Hood plaintiffs were entitled to and did rely on the Mt. Hood defendants' representations, as described herein, and would not have purchased any interests in the Mt. Hood limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

199. The Mt. Hood plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

200. The Mt. Hood plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Mt. Hood plaintiffs and conceal the

fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 196-197 above. If the Mt. Hood plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 196-197 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

201. The Mt. Hood plaintiffs hereby tender their limited partnership interests to the Mt. Hood defendants.

• • •

COUNT II

(1934 Securities Exchange Act - Section 10(b))

208. The Mt. Hood plaintiffs reallege and incorporate by reference paragraphs 1-31 and 188-201 above.

209. In connection with the sale of the limited partnership interests in Mt. Hood Associates, defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf (the "Mt. Hood primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Mt. Hood plaintiffs; made untrue statements of material fact, as described in paragraphs 192-193 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 194 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Mt. Hood plaintiffs.

210. The Mt. Hood primary violators, and each of them, knew of the falsity of the representations described in paragraph 192 above, or recklessly failed to ascertain the

truth of the representations. The Mt. Hood primary violators knew of the omissions of material fact described in paragraph 194 above, or recklessly failed to disclose these facts.

211. Defendants ACE, Analysis, Hernandez, Chandler, Anico, Johnson, TexCom, Buhler, Buhler Software, P-Stat, ConServ, and Steinberger (the "Mt. Hood aiders and abettors"), knew that their actions, as described in paragraphs 189b-f and 195 above, furthered and provided substantial assistance to the primary violators in committing a fraud on the Mt. Hood plaintiffs.

212. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5

213. As a result of these acts, the Mt. Hood plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

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FOURTH CLAIM FOR RELIEF -
COLUMBIA ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Columbia plaintiffs.

268. The Columbia plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

269. The following plaintiffs invested in the Columbia Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Columbia plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Dale R. Peterson	12/80	$26,805
Earl D. Riddle	12/80	26,805
Jack E. Evans	12/80	26,805
Robert E. Johnsen	12/80	26,805
Harlan C. Selby	12/80	26,805
Charles W. Botsford	12/80	26,805
Walter L. Beers	12/80	26,805
R. Matison White	12/30/80	26,805
William L. Gunnell	12/80	26,805
Harry E. Groth, Jr.	12/80	26,805

270. The following defendants participated in the Columbia Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Columbia defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Columbia partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Columbia Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Columbia defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print,

and distribute a model offering memorandum on which the Columbia offering memorandum was based and prepare, print, and distribute a model partnership agreement and model sales and lease agreements on which the Columbia partnership agreement and sales and lease agreements were based; and

(7) instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, defendant LCI was aslo the immediate seller for the Columbia partnership. As described in paragraph 6a above, in this capacity, LCI was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Columbia equipment") purportedly consisted of two IBM 370/158 CPU's, an IBM 3800 Printing Subsystem, and approximately thirteen pieces of IBM peripheral equipment. The Columbia partnership was to pay a total of $1.45 million for this equipment. The master tape was of a software program known as Office Automation System ("OAS"), which was purportedly specially designed to perform basic accounting functions, such as payroll and receivables, on Xerox and Wang word processing units, and was purportedly readily marketable to businesses having those makes of word processing units. The Columbia partnership was to pay a total of $1.95 million for this master tape. Defendants McKenna, Heitmeyer, Wellbrock, and Ward were principals and controlling persons of defendant LCI. LCI played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by purchasing the Columbia equipment and the OAS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Columbia partnership, it obscured the original purchase price

of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCI was or should have been aware of its integral role in the Columbia offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. LCI knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Analysis was the equipment seller/lessee for the Columbia partnership. As described in paragraph 6a above, in this capacity, Analysis was the entity that sold the Columbia equipment to the immediate seller, LCI, for resale to the Columbia partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end users, which were represented to be W.R. Grace & Company, Westinghouse Electric Corporation, and Spring Mills, Inc., and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in

that, by selling the Columbia equipment to LCI for resale to the Columbia partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCI had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end-user lease terms described in the Columbia offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/lease-back scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Columbia offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Analysis knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life and residual value of the equipment.

d. Defendant SSWPI was the master tape lessee for the Columbia partnership. As described in paragraph 6b above, in this capacity, SSWPI was the entity that leased the OAS master tape back from the Columbia partnership and was to market and obtain licensees for the use of the master tape. Defendant SSWPI was an affiliate of Rosen

Associates, which was the master tape seller for the Columbia partnership. As described in paragraph 6b above, in this capacity, Rosen Associates was the entity that sold the OAS master tape to LCI, the immediate seller, for resale to the Columbia partnership. Defendant Rosen was the owner and controlling person of Rosen Associates and SSWPI. Rosen Associates, SSWPI, and/or Rosen had purportedly developed the OAS software program and had purported expertise in marketing the OAS master tape. On information and belief, Rosen formed Rosen Associates and/or SSWPI solely for purposes of participating in the Columbia partnership. Rosen Associates and Rosen played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by selling the OAS master tape to LCI for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCI had purchased the tape from an independent third party in an arm's length, negotiated transaction. SSWPI and Rosen played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by virtue of their purported expertise in the OAS software program and in the marketing of this software, they appeared capable of successfully exploiting the OAS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Rosen Associates, SSWPI, and Rosen were or should have been aware of their integral role in the Columbia offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the OAS master tape would be used by the packagers in a limited partnership offering. Rosen Associates, SSWPI, and Rosen knew or should have known that the OAS master tape transactions described herein would be used to induce the investors to invest in

the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the OAS master tape.

e. Defendant Computer Value was the equipment appraiser for the Columbia partnership. Defendant Cuthbert was the president and controlling person of Computer Value. Defendants Computer Value and Cuthbert prepared a written appraisal of the Columbia equipment, on or about September 29, 1980 (hereinafter "the Cuthbert-Columbia appraisal"), which appeared in the Columbia offering memorandum, and which represented that the Columbia equipment had a fair market value of $1.5 million, a useful life in excess of nine years, and a residual value at the end of nine years in excess of $300,000. Computer Value and Cuthbert played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, the Cuthbert-Columbia appraisal justified the inflated price the partnership was to pay for the Columbia equipment and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end-user leases, from which the partnership would derive bonus rentals. Computer Value and Cuthbert were or should have been aware that the Cuthbert-Columbia appraisal would be disseminated to prospective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Cuthbert-Columbia appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Columbia equipment.

f. Defendant TMS was the master tape appraiser for the Columbia partnership. Defendant Turi was the president and controlling person of TMS. Defendants TMS and Turi prepared a written appraisal of the OAS master tape, on or about October 31, 1980 (hereinafter "the TMS-Columbia appraisal"), which appeared in the Columbia offering memorandum, and which represented that the fair market value of the OAS master tape to be purchased from Rosen Associates and leased to SSWPI was in excess of $3.4 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Columbia partnership was paying for the OAS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Turi had met with the management and technical staff of Rosen Associates and SSWPI, had examined in detail the contents of the OAS master tape, and had discussed with Rosen Associates and SSWPI the underlying objectives of the OAS program, its current development and operational status, the marketing plans contemplated by SSWPI, and the market segments that could benefit from licensing the OAS master tape. TMS and Turi played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that the TMS-Columbia appraisal justified the inflated price the partnership was to pay for the OAS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the OAS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. TMS and Turi were or should have been aware that the TMS-Columbia appraisal would be disseminated to prospective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the TMS-Columbia appraisal in making their investment decisions, and to substantiate, for tax

purposes, the fair market value and useful life of the OAS master tape.

g. Defendant Lampf was the special tax counsel for the Columbia partnership. In this capacity, Lampf issued a special written tax opinion for the Columbia partnership, in or about October 1980 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Columbia offering memorandum, and upon which it knew potential investors, including the Columbia plaintiffs, would rely in making their investment in Columbia Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Columbia Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Columbia offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model sale and lease agreements, on which the Columbia partnership agreement and sale and lease agreements were based.

271. Beginning in or around November 1980, and continuing to the present, the Columbia defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Columbia plaintiffs in connection with the sale of limited partnership interests in Columbia Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and lease-back the Columbia computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Columbia investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

272. The Columbia plaintiffs were induced to invest in Columbia Associates by means of an offering memorandum dated November 14, 1980, and a supplemental offering memorandum dated December 29, 1980 (hereinafter collectively "the Columbia offering memorandum"), which included the Lampf tax opinion, the Cuthbert-Columbia appraisal, and the TMS-Columbia appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 270b above, the end users that were purportedly already leasing this equipment, as described in paragraph 270c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 270b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 270e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Turi, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

273. The Columbia offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Columbia partnership had been, or would be, involved. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants in the Columbia partnership had been, or would be, involved.

274. In connection with the sale of interests in Columbia Associates to the Columbia plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated from licensing the OAS master tape and from the lease income and residual value in the Columbia equipment;

b. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investor's entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the Columbia equipment existed, was specifically identified, and was already under lease to W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc. on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the OAS master tape program was ready to be marketed in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the OAS master tape program was tangible, new and original and previously unexploited property, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that SSWPI and Rosen Associates, the master tape lessee and its affiliate, despite their small size, were skilled enough

and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the OAS master tape and thereby generate revenues for the Columbia partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that Turi had met with the management and staff of Rosen Associates and SSWPI, and had become familiar with the contents and operation of the OAS program and the marketing potential of the OAS master tape;

h. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the fair market value, residual value, and useful life attributed to the Columbia equipment were reasonable and accurate;

i. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the fair market value and useful life attributed to the OAS master tape were reasonable and accurate.

275. These representations were false and misleading in that:

a. The IBM computer equipment described in the Columbia offering memorandum did not exist or was not under lease to the end users, W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., as represented;

b. The profits promised in the Columbia offering memorandum and in the Lampf tax opinion could not be realized by the Columbia plaintiffs;

c. The actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented;

d. The actual fair market value and useful life of OAS master tape were substantially less than represented;

e. The OAS master tape was not readily marketable in its target market without substantial modifications in format;

f. On information and belief, the OAS master tape program was not tangible, new, original or previously unexploited property, and therefore not qualified for investment tax credit;

g. Rosen Associates and SSWPI did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the OAS master tape;

h. On information and belief, before issuing the TMS-Columbia appraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the OAS master tape.

276. In making the representations described above, the following Columbia defendants failed to disclose the following material facts to the Columbia plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Columbia offering memorandum was not in fact the equipment owned by LCI or Analysis and purchased by the partnership;

b. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the IBM equipment described in the Columbia offering memorandum was not currently under lease to W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., the purported end users;

c. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented in the Columbia offering memorandum and in the Cuthbert-Columbia appraisal;

d. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that they had not performed any investigation to examine the Columbia equipment or to verify its existence and condition;

e. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the Columbia IBM equipment was essentially obsolete at the time it was purchased by the Columbia partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, TMS, and Turi failed to disclose that the actual market value and useful life of the OAS master tape were substantially less than represented in the Columbia offering memorandum and in the TMS-Columbia appraisal;

g. The packagers, Lampf, TMS, and Turi failed to disclose that the TMS-Columbia appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Lampf, TMS, and Turi failed to disclose that before issuing the TMS-Columbia appraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the OAS master tape;

i. The packagers, Lampf, TMS and Turi failed to disclose that, in order to achieve the market share projected in the TMS-Columbia appraisal, the expenses of marketing the OAS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

j. The packagers, Lampf, TMS, and Turi failed to disclose that Rosen Associates and SSWPI were undercapi-

talized and without sufficient skill, expertise, and personnel to market and license the OAS master tape and general revenues for the partnership;

k. the packagers, Lampf, TMS, and Turi failed to disclose that the OAS master tape was not readily marketable in its target market without substantial modifications in format; and

l. The packagers, Lampf, Analysis, Computer Value, and Cuthbert failed to disclose that the Columbia partnership would not and coulod not obtain title Columbia equipment because of the terms and nature of pre-existing transactions involving the Columbia equipment.

277. Defendants Cuthbert, Computer Value, TMS, Turi, LCI, Analysis, Hernandez, Chandler, Anico, Rosen Associates, SSWPI, and Rosen aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Columbia partnership and their actions in furtherance of these roles, as described in paragraphs 270b-f above, were essential components of the fraud perpetrated on the Columbia plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Columbia plaintiffs.

278. Beginning in and around November 1980, and continuing until the present, the Columbia defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around April 1981, the packager defendants arranged for Mr. Turi to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Columbia plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Columbia equipment lease were current and that diligent efforts were being made to market and obtain licensees for the OAS master

tape when, in fact, equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

279. The Columbia plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Columbia defendants, as described herein. The Columbia plaintiffs had no reason to believe that the Columbia defendants omitted to state material facts, as described herein. The Columbia plaintiffs were not aware of the true facts or the facts that the Columbia defendants omitted to state. The Columbia plaintiffs were entitled to and did rely on the Columbia defendants' representations, as described herein, and would not have purchased any interests in the Columbia limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

280. The Columbia plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

281. The Columbia plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Columbia plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 278 above. If the Columbia plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs

8 and 278 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

282. The Columbia plaintiffs hereby tender their limited partnership interests to the Columbia defendants.

• • •

COUNT II

(1934 Securities Exchange Act - Section 10(b))

289. The Columbia plaintiffs reallege and incorporate by reference paragraphs 1-31 and 269-282 above.

290. In connection with the sale of the limited partnership interests in Columbia Associates, defendants LCI, LCA, McKenna, Wellbrock, Ward, and Lampf (the "Columbia primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Columbia plaintiffs; made untrue statements of material fact, as described in paragraph 274-275 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 276 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Columbia plaintiffs.

291. The Columbia primary violators, and each of them, knew of the falsity of the representations described in paragraph 274 above, or recklessly failed to ascertain the truth of the representations. The Columbia primary violators knew of the omissions of material fact described in paragraph 276 above, or recklessly failed to disclose these facts.

292. Defendants Analysis, Hernandez, Chandler, Anico, LCI, Computer Value, Cuthbert, Rosen Associates, SSWPI,

Rosen, TMS, and Turi (the Columbia "aiders and abettors") knew that their actions, as described in paragraphs 270b-f and 277 above, furthered and provided substantial assistance to the Columbia primary violators in committing a fraud on the Columbia plaintiffs.

293. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

294. As a result of these acts, the Columbia plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

FIFTH CLAIM FOR RELIEF - SALEM ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Salem plaintiffs.

349. The Salem plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

350. The following plaintiffs invested in the Salem Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Salem plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Dale R. Peterson	12/22/80	$25,227
Jack E. Evans	12/80	25,227
Harlan C. Selby	12/22/80	25,227
Ronald Kirkilie	12/22/80	25,227
Deane E. Reiman	12/24/80	25,227
Jerry E. Marks	12/31/80	25,227
Robert Callahan	12/30/80	25,227
Elman Peterson, Jr.	12/31/80	25,227
Joseph C. Player	12/30/80	25,227
Floyd E. Hambleton	12/30/80	25,227
Woodrow Gwyn	12/80	25,227
Ethel Nunemacher	12/29/80	25,227
C. Wayne Warren	12/80	25,227

351. The following defendants participated in the Salem Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Salem defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Salem partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Salem Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Salem defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Salem offering memorandum was based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements, on which the Salem partnership agreement and sales and lease agreements were based; and

(7) Instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, defendant LCI was also the immediate seller for the Salem partnership. As described in paragraph 6 above, in this capacity, LCI was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Salem equipment") purportedly consisted of three IBM 3800 Printing Subsystems. The Salem partnership was to pay a total of $1.115 million for this equipment. The master tape was of a software program known as Insurance Brokers and Agents System ("IBAS"), which was purportedly specially designed for use by insurance offices to perform routine administrative and accounting functions, and was purportedly readily marketable within that industry. The Salem partnership was to pay a total of $1.9 million for this master tape. Defendants McKenna, Heitmeyer, Wellbrock, and Ward were principals and controlling persons of defendant LCI. LCI played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by purchasing the Salem equipment and the IBAS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Salem partnership, it obscured the original purchase price of the equipment and master tape, provided a means

by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCI was or should have been aware of its integral role in the Salem offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment or master tape would be used by the packagers in a limited partnership offering. LCI knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Analysis was the equipment seller/lessee for the Salem partnership. As described in paragraph 6a above, in this capacity, Analysis was the entity that sold the IBM equipment to the immediate seller, LCI, for resale to the Salem partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end user, which was represented to be the Coleman Company, and was to re-lease the equipment to a subsequent end user when the existing user lease expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by selling the Salem equipment to LCI for resale to the Salem partnership, it further

obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCI had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end-user lease terms described in the Salem offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Salem offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Analysis knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life and residual value of the equipment.

d. Defendant Applications was the master tape lessee for the Salem partnership. As described in paragraph 6b above, in this capacity, Applications was the entity that leased the IBAS master tape back from the Salem partnership and was to market and obtain licensees for the use of the master tape. Defendant Applications was an affiliate of ASG, which was the master tape seller for the Salem partnership. As described in paragraph 6b above,

in this capacity, ASG was the entity that sold the IBAS master tape to LCI, the immediate seller, for resale to the Salem partnership. Defendant Pine was the president and controlling person of ASG and Applications. ASG, Applications, and/or Pine had purportedly developed the IBAS software program and had purported expertise in marketing the IBAS master tape. On information and belief, Pine formed ASG and/or Applications solely for purposes of participating in the Salem partnership. ASG and Pine played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by selling the IBAS master tape to LCI for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCI had purchased the tape from an independent third party in an arm's length, negotiated transaction. Applications and Pine played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by virtue of their purported expertise in the IBAS software program and in the marketing of this software, they appeared capable of successfully exploiting the IBAS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. ASG, Applications, and Pine were or should have been aware of their integral role in the Salem offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the IBAS master tape would be used by the packagers in a limited partnership offering. ASG, Applications, and Pine knew or should have known that the IBAS master tape transactions described herein would be used to induce the investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to

substantiate, for tax purposes, the fair market value and useful life of the IBAS master tape.

e. Defendant Global was the equipment appraiser for the Salem partnership. Defendant Johnson was the president, owner, and controlling person of Global. Defendants Global and Johnson prepared a written appraisal of the Salem equipment, on or about November 24, 1980 (hereinafter "the Global appraisal"), which appeared in the Salem offering memorandum, and which represented that the Salem equipment had a fair market value in excess of $1.115 million, that it had a useful life of nine years, and that at the end of nine years, it would have a residual value of $225,000. Global and Johnson played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that the Global appraisal justified the inflated price the partnership was to pay for the Salem equipment and provided the limited partners with "independent" substantiation for the assumptions in the Salem offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end-user leases, from which the partnership would derive bonus rentals. Global and Johnson were or should have been aware that the Global appraisal would be disseminated to prospective investors in Salem Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Global appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Salem equipment.

f. Defendant TMS was the master tape appraiser for the Salem partnership. Defendant Turi was the president and controlling person of TMS. Defendants TMS and Turi prepared a written appraisal of the IBAS master tape, on or about November 26, 1980 (hereinafter "the TMS-Salem

appraisal"), which appeared in the Salem offering memorandum, and which represented that the IBAS master tape to be purchased from ASG and leased to Applications had a fair market value in excess of $2.19 million and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Salem partnership was paying for the IBAS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Turi had met with the management and technical staff of ASG and Applications, had examined in detail the contents of the IBAS master tape, and had discussed with ASG and Applications the underlying objectives of the IBAS program, its current development and operational status, the marketing plans contemplated by Applications, and the market segments that could benefit from licensing the IBAS master tape. TMS and Turi played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that the TMS-Salem appraisal justified the inflated price the partnership was to pay for the IBAS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Salem offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the IBAS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. TMS and Turi were or should have been aware that the TMS-Salem appraisal would be disseminated to prospective investors in Salem Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the TMS-Salem appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the IBAS master tape.

g. Defendant Lampf was the special tax counsel for the Salem partnership. In this capacity, Lampf issued a special written tax opinion for the Salem partnership, in

or about December 1980 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Salem offering memorandum, and upon which it knew potential investors, including the Salem plaintiffs, would rely in making their investment in Salem Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Salem Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Salem offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Salem Associates partnership agreement and sales and lease agreements were based.

352. Beginning in or around December 1980, and continuing to the present, the Salem defendants in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Salem plaintiffs in connection with the sale of limited partnership interests in Salem Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Salem computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Salem investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

353. The Salem plaintiffs were induced to invest in Salem Associates by means of an offering memorandum dated December 4, 1980 (hereinafter "the Salem offering memorandum"), which included the Lampf tax opinion, the Global appraisal, and the TMS-Salem appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 351b above,

the end user that was purportedly already leasing this equipment, as described in paragraph 351c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 351b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 351e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Turi, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

354. The Salem offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Salem partnership had been, or would be, involved. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants in the Salem partnership had been, or would be, involved.

355. In connection with the sale of interests in Salem Associates to the Salem plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated from licensing the IBAS master tape and from the lease income and residual value in the Salem equipment;

b. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement

to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and Global and Johnson, in the Global appraisal, represented that the Salem equipment existed, was specifically identified, and was already under lease to the Coleman Company on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that the IBAS master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the IBAS master tape program was tangible, new, original and previously unexploited property, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that Applications and ASG, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the IBAS master tape and thereby generate revenues for the Salem partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that Turi had met with the management and staff of ASG and Applications, and had become familiar with the contents and

operation of the IBAS program and the marketing potential of the IBAS master tape;

h. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and Global and Johnson, in the Global appraisal, represented that the fair market value, residual value, and useful life attributed to the Salem equipment were reasonable and accurate;

i. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that the fair market value and useful life attributed to the IBAS master tape were reasonable and accurate.

356. These representations were false and misleading in that:

a. The IBM computer equipment described in the Salem offering memorandum did not exist or was not under lease to the end user, the Coleman Company, as represented;

b. The profits promised in the Salem offering memorandum and in the Lampf tax opinion could not be realized by the Salem plaintiffs;

c. The actual fair market value, residual value, and useful life of the Salem equipment were substantially less than represented;

d. The actual fair market value and useful life of the IBAS master tape were substantially less than represented;

e. The IBAS master tape was not readily marketable in its target market without substantial modifications in format;

f. On information and belief, the IBAS master tape program was not tangible, new, original or previously unexploited property, and therefore not qualified for investment tax credit;

g. ASG and Applications did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the IBAS master tape;

h. On information and belief, before issuing the TMS-Salem appraisal, Turi had not met with the management and staff of ASG and Applications, had not tested or run the IBAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the IBAS master tape.

357. In making the representations described above, the following Salem defendants failed to disclose the following material facts to the Salem plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Salem offering memorandum was not in fact the equipment owned by LCI or Analysis and purchased by the partnership;

b. The packagers, Lampf, Global, and Johnson failed to disclose that the IBM equipment described in the Salem offering memorandum was not currently under lease to the Coleman Company, the purported end user;

c. The packagers, Lampf, Global, and Johnson failed to disclose that the actual fair market value, residual value, and useful life of the Salem equipment were substantially less than represented in the Salem offering memoranda and in the Global appraisal;

d. The packagers, Lampf, Global, and Johnson failed to disclose that they had not performed any investigation to examine the Salem equipment or to verify its existence and condition;

e. The packagers, Lampf, Global, and Johnson failed to disclose that the Salem IBM equipment was essentially obsolete at the time it was purchased by the Salem partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, TMS, and Turi failed to disclose that the actual fair market value and useful life of IBAS master tape were substantially less than represented in the Salem offering memorandum and in the TMS-Salem appraisal;

g. The packagers, Lampf, TMS, and Turi failed to disclose that the IBAS master tape was not readily marketable in its target market without substantial modifications in format;

h. The packagers, Lampf, TMS, and Turi failed to disclose that the TMS-Salem appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

i. The packagers, Lampf, TMS, and Turi failed to disclose that before issuing the TMS-Salem appraisal, Turi had not met with the management and staff of ASG and Applications, had not tested or run the IBAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the IBAS master tape;

j. The packagers, Lampf, TMS, and Turi failed to disclose that, in order to achieve the market share projected in the TMS-Salem appraisal, the expenses of marketing the IBAS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

k. The packagers, Lampf, TMS, and Turi failed to disclose that ASG and Applications were undercapitalized and without sufficient skill, expertise, and personnel to market and license the IBAS master tape and generate revenues for the partnership; and

l. The packagers, Lampf, Analysis, Global and Johnson failed to disclose that the Salem plaintiffs would not and could not obtain title to the Salem equipment because of

the terms and nature of pre-existing transactions involving the Salem equipment.

358. Defendants Johnson, Global, TMS, Turi, LCI, Analysis, Hernandez, Chandler, Anico, ASG, Applications, and Pine aided and abetted the misrepresentations and omissions alleged above in that their roles in the Salem partnership and their actions in furtherance of these roles, as described in paragraphs 351b-f above, were essential components of the fraud perpetrated on the Salem plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Salem plaintiffs.

359. Beginning in and around December 1980, and continuing until the present, the Salem defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around April 1981, the packager defendants arranged for Mr. Turi to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Salem plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Salem equipment lease were current and that diligent efforts were being made to market and obtain licensees for the IBAS master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

360. The Salem plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Salem defendants, as described herein. The Salem plaintiffs had no reason to believe that the Salem

defendants omitted to state material facts, as described herein. The Salem plaintiffs were not aware of the true facts or the facts that the Salem defendants omitted to state. The Salem plaintiffs were entitled to and did rely on the Salem defendants' representations, as described herein, and would not have purchased any interests in the Salem limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

361. The Salem plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

362. The Salem plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Salem plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 359 above. If the Salem plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 359 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

363. The Salem plaintiffs hereby tender their limited partnership interests to the Salem defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b))

370. The Salem plaintiffs reallege and incorporate by reference paragraphs 1-31 and 350-363 above.

371. In connection with the sale of limited partnership interests in Salem Associates, defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf (the "Salem primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Salem plaintiffs; made untrue statements of material fact, as described in paragraphs 355-356 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 357 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Salem plaintiffs.

372. The Salem primary violators, and each of them, knew of the falsity of the representations described in paragraph 355 above, or recklessly failed to ascertain the truth of the representations. The Salem primary violators knew of the omissions of material fact described in paragraph 357 above, or recklessly failed to disclose these facts.

373. Defendants Analysis, Hernandez, Chandler, Anico, LCI, Global, Johnson, ASG, Applications, Pine, TMS, and Turi (the "Salem aiders and abettors") knew that their actions, as described in paragraphs 351b-f and 358 above, furthered and provided substantial assistance to the Salem primary violators in committing a fraud on the Salem plaintiffs.

374. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

375. As a result of these acts, the Salem plaintiffs are entitled to recover damages equal to all sums paid for

their investment, together with interest thereon since the date paid.

* * *

SIXTH CLAIM FOR RELIEF - EUSTON ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Euston plaintiffs.

430. The Euston plaintiffs reallege and incorporate by reference paragraphs 1-31 above.

431. The following plaintiffs invested in the Euston Associates limited partnership in the amounts and on the dates indicated below. They shall be referred herein as the "Euston plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Dale R. Peterson	06/08/81	$29,460
Harlan C. Selby	06/08/81	29,460
Perry Coleman	06/05/81	14,730
Bruce Sigman	05/26/81	29,460
Ronald and Joan Chatham	06/08/81	14,730
David Collier	06/08/81	29,460
H. Winston Marshall	06/03/81	29,460
Arlyss D. Dunham	06/05/81	29,460
Robert E. Boekenoogen	06/09/81	29,460
Robert W. Chambers	06/81	58,920
Cliff B. Chulos	06/02/81	29,460
Jay L. Maxwell and James R. McDonald	06/10/81	14,730
Larry G. Zettle	06/10/81	29,460
David McCullam	06/02/81	58,920
John Ball	06/12/81	29,460

432. The following defendants participated in the Euston Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Euston defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Euston partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Euston Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Euston defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of defendant Lampf to act as special tax counsel for the partnership and to render a tax opinion for the partnership;

(7) Instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant LCA was the immediate seller for the Euston partnership. As described in paragraph 6a above, in this capacity, LCA was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Euston equipment") purportedly consisted of an IBM 3032-6 CPU and associated power and console equipment, and approximately seven pieces of IBM peripheral equipment. The Euston partnership was to pay a total of $1,566,154 for this equipment. The master tape was of a software program known as Real Estate Management System ("REMS"), which was purportedly

specially designed for use in the real estate management market for tenant control, accounts receivable and property management and readily marketable within that market and industry. The Euston partnership was to pay a total of $2.2 million for this master tape. Defendant LCA was comprised of defendants McKenna, Heitmeyer, and Wellbrock. LCA played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that, by purchasing the Euston equipment and the REMS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Euston partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCA was or should have been aware of its integral role in the Euston offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and which knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. LCA knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Comdisco was the equipment seller/lessee for the Euston partnership. As described in paragraph 6a above, in this capacity, Comdisco was the entity that sold the IBM equipment to the immediate seller, LCA, for re-

sale to the Euston partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end users, which were represented to be Levi Strauss and Control Data, and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Defendant Pontikes was an officer and controlling person of Comdisco. Comdisco played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that, by selling the Euston equipment to LCA for resale to the Euston partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCA had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Comdisco also added credence to the reasonableness of the end-user lease terms described in the Euston offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Comdisco also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end-user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Comdisco was or should have been aware of its integral role in the Euston offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Comdisco knew or should have known the equipment transactions described herein would be used to induce these investors to invest in the partnership, and that the investors would rely on the terms of the transactions in

making their investment decisions, and to substantiate, for tax purposes, the fair market value, title, useful life and residual value of the equipment.

d. An entity known as Prose, Inc. was the master tape lessee for the Euston partnership. As described in paragraph 6b above, in this capacity, Prose was the entity that leased the REMS master tape back from the Euston partnership and was to market and obtain licensees for the use of the master tape. An entity known as M.A. Hanson & Associates was an affiliate of Prose and was the master tape seller for the Euston partnership. As described in paragraph 6b above, in this capacity, M.A. Hanson & Associates was the entity that sold the REMS master tape to LCA, the immediate seller, for resale to the Euston partnership. Defendant Mark Hanson was the owner, officer, and controlling person of Prose and M.A. Hanson & Associates. Prose, M.A. Hanson & Associates, and/or defendant Hanson had purportedly developed the REMS software program and had purported expertise in marketing the REMS master tape. On information and belief, defendant Hanson formed Prose and/or M.A. Hanson & Associates solely for purposes of participating in the Euston offering. Hanson played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that, by selling the REMS master tape to LCA for resale to the partnership, he made the purchase price of the tape appear reasonable by making it appear as if LCA had purchased the tape from an independent third party in an arm's length, negotiated transaction. Hanson, Prose, and M.A. Hanson & Associates played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that, by virtue of their purported expertise in the REMS software program and in the marketing of this software, they appeared capable of successfully exploiting the REMS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated

valuation of the tape. Hanson, Prose, and M.A. Hanson & Associates were or should have been aware of their integral role in the Euston offering and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the REMS master tape would be used by the packagers in a limited partnership offering. Hanson, Prose, and M.A. Hanson & Associates knew or should have known that the REMS master tape transactions described herein would be used to induce the investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the REMS master tape.

e. Defendant Computer Value was the equipment appraiser for the Euston partnership. Defendant Cuthbert was the president and controlling person of Computer Value. Defendants Computer Value and Cuthbert prepared a written appraisal of the Euston equipment, in or about April 1981 (hereinafter "the Cuthbert-Euston appraisal"), which appeared in the Euston offering memorandum, and which represented that the Euston equipment had a fair market value in excess of $2.03 million, that it had a useful life of nine years, and that at the end of the nine years, it would have a residual value of at least $403,000. Computer Value and Cuthbert played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that, the Cuthbert-Euston appraisal justified the inflated price the partnership was to pay for the Euston equipment and provided the limited partners with "independent" substantiation for the assumptions in the Euston offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after

the expiration of the end-user leases, from which the partnership would derive bonus rentals. Computer Value and Cuthbert were or should have been aware that the Cuthbert-Euston appraisal would be disseminated to prospective investors in Euston Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Cuthbert-Euston appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Euston equipment.

f. Defendant Edward G. Fizell was the master tape appraiser for the Euston partnership. Defendant Fizell prepared a written appraisal of the REMS master tape, on or about April 10, 1981 (hereinafter "the Fizell appraisal"), which appeared in the Euston offering memorandum, and which represented that the REMS master tape to be purchased from M.A. Hanson & Associates and leased to Prose had a fair market value in excess of $2.6 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Euston partnership was paying for the REMS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Fizell had met with the management of M.A. Hanson & Associates and Prose, had examined in depth the design and structure of the REMS program, and had conducted an independent review of the potential market for the REMS master tape. Defendant Fizell played an integral and essential role in the fraud perpetrated upon the Euston plaintiffs in that the Fizell appraisal justified the inflated price the partnership was to pay for the REMS master tape and provide the limited partners with "independent" substantiation for the assumptions in the Euston offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the REMS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at

least nine years. Fizell was or should have been aware that the Fizell appraisal would be disseminated to prospective investors in Euston Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Fizell appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the REMS master tape.

g. Defendant Lampf was the special tax counsel for the Euston partnership. In this capacity, Lampf issued a special written tax opinion for the Euston partnership, in or about April 1981 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Euston offering memorandum, and upon which it knew potential investors, including the Euston plaintiffs, would rely in making their investment in Euston Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Euston Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Euston offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and partnership sales and lease agreements, on which the Euston Associates partnership agreement and sales and lease agreements were based.

433. Beginning in or around April 1981, and continuing to the present, the Euston defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Euston plaintiffs in connection with the sale of limited partnership interests in Euston Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Euston computer equipment and master tape described above. This

program was purportedly designed to generate substantial tax benefits to the Euston investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

434. The Euston plaintiffs were induced to invest in Euston Associates by means of an offering memorandum dated April 10, 1981 (hereinafter "the Euston offering memorandum"), which included the Lampf tax opinion, the Cuthbert-Euston appraisal, and the Fizell appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 432b above, the end users that were purportedly already leasing this equipment, as described in paragraph 432c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 432b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 432e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Fizell, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

435. The Euston offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Euston partnership had been, or would be, involved.

436. In connection with the sale of interests in Euston Associates to the Euston plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, represented that

the limited partnership investment would provide substantial profits resulting from fees generated from licensing the REMS master tape and from the lease income and residual value in the Euston equipment;

b. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Euston appraisal, represented that the Euston equipment existed, was specifically identified, and was already under lease to Levi Strauss and Control Data on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Fizell, in the Fizell appraisal, represented that the REMS master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, represented that the REMS master tape program was tangible, new, original and previously unexploited property, and therefore qualified for investment tax credit;

f. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Fizell, in the Fizell appraisal, represented that Prose and M.A. Hanson & Associates, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the REMS master tape and thereby generate revenues for the Euston

partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Fizell, in the Fizell appraisal, represented that Fizell had met with the management of M.A. Hanson & Associates and Prose, had become familiar with the design and structure of the REMS program, and had conducted independent research into the marketability of the REMS master tape;

h. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Euston appraisal, represented that the fair market value, residual value, and useful life attributed to the Euston equipment were reasonable and accurate;

i. The packagers and Lampf, in the Euston offering memorandum and the Lampf tax opinion, and Fizell, in the Fizell appraisal, represented that the fair market value and useful life attributed to the REMS master tape were reasonable and accurate.

437. These representations were false and misleading in that:

a. The profits promised in the Euston offering memorandum and in the Lampf tax opinion could not be realized by the Euston plaintiffs;

b. The actual fair market value, residual value, and useful life of the Euston equipment were substantially less than represented;

c. The actual fair market value and useful life of the REMS master tape were substantially less than represented;

d. The REMS master tape was not readily marketable in its target market without substantial modifications in format;

e. On information and belief, the REMS master tape program was not tangible, new, original or previously unexploited property, and therefore not qualified for investment tax credit;

f. Prose and M.A. Hanson & Associates did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the REMS master tape;

g. On information and belief, before issuing the Fizell appraisal, Fizell had not met with the management of Prose and M.A. Hanson & Associates, had not tested or run the REMS program and was not familiar with its design and structure, and had not independently or adequately researched the marketability of the REMS master tape.

438. In making the representations described above, the following Euston defendants failed to disclose the following material facts to the Euston plaintiffs:

a. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the actual fair market value, residual value, and useful life of the Euston equipment were substantially less than represented in the Euston offering memorandum and in the Cuthbert-Euston appraisal;

b. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the Euston IBM equipment was essentially obsolete at the time it was purchased by the Euston partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

c. The packagers, Lampf, and Fizell failed to disclose that the actual fair market value and useful life of the REMS master tape program were substantially less than represented in the Euston offering memorandum and in the Fizell appraisal;

d. The packagers, Lampf, and Fizell failed to disclose that the REMS master tape appraisal contained income

projections for valuation purposes that were made without a reasonable basis in fact;

e. The packagers, Lampf, and Fizell failed to disclose that before issuing the Fizell appraisal, Fizell had not met with the management of Prose and M.A. Hanson & Associates, had not tested or run the REMS program and was not familiar with its design and structure, and had not independently or adequately researched the marketability of the REMS master tape;

f. The packagers, Lampf, and Fizell failed to disclose that the REMS master tape was not readily marketable in its target market without substantial modifications in format;

g. The packagers, Lampf, and Fizell failed to disclose that, in order to achieve the market share projected in the Fizell appraisal, the expenses of marketing the REMS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

h. The packagers, Lampf, and Fizell failed to disclose that Prose and M.A. Hanson & Associates were undercapitalized and without sufficient skill, expertise, and personnel to market and license the REMS master tape and generate revenues for the partnership; and

i. The packagers, Lampf, Comdisco, Computer Value and Cuthbert failed to disclose that the Euston plaintiffs would not and could not obtain title to the Euston equipment because of the terms and nature of pre-existing transactions involving the Euston equipment.

439. Defendants Cuthbert, Computer Value, Fizell, Comdisco, Pontikes, and Hanson aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Euston partnership and their actions in furtherance of these roles, as described in paragraphs 432b-

f above, were essential components of the fraud perpetrated on the Euston plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Euston plaintiffs.

440. Beginning in and around April 1981, and continuing until the present, the Euston defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around September 1981, the packager defendants arranged for Mr. Fizell to be replaced by The Lawrence Group to act as consultant to the partnership and continually assure and represented to the Euston plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Euston equipment lease were current and that diligent efforts were being made to market and obtain licensees for the REMS master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

441. The Euston plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Euston defendants, as described herein. The Euston plaintiffs had no reason to believe that the Euston defendants omitted to state material facts, as described herein. The Euston plaintiffs were not aware of the true facts or the facts that the Euston defendants omitted to state. The Euston plaintiffs were entitled to and did rely on the Euston defendants' representations, as described herein, and would not have purchased any interests in the Euston limited partnership had the misrepresentations of

material facts not been made or had the omissions of material facts not occurred.

442. The Euston plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

443. The Euston plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and defendant Lampf attempted to and did mislead the Euston plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 440 above. If the Euston plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and defendant Lampf, as described in paragraphs 8 and 440 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

444. The Euston plaintiffs hereby tender their limited partnership interests to the Euston defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b))

451. The Euston plaintiffs reallege and incorporate by reference paragraphs 1-31 and 431-444 above.

452. In connection with the sale of the limited partnership interests in Euston Associates, defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf (the "Euston primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities

of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Euston plaintiffs; made untrue statements of material fact, as described in paragraphs 436-437 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 438 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate as a fraud and deceit upon the Euston plaintiffs.

453. The Euston primary violators, and each of them, knew of the falsity of the representations described in paragraph 436 above, or recklessly failed to ascertain the truth of the representations. The Euston primary violators knew of the omissions of material fact described in paragraph 438 above, or recklessly failed to disclose these facts.

454. Defendants Comiisco, Potikes, Hanson, Computer Value, Cuthbert, and Fizell (the "Euston aiders and abettors") knew that their actions, as described in paragraphs 432b-f and 439 above, furthered and provided substantial assistance to the Euston primary violators in committing a fraud on the Euston plaintiffs.

455. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

456. As a result of these acts, the Euston plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

COMPLAINT IN *GILBERTSON, et al.* V. *LEASING CONSULTANTS ASSOCIATES, et al.*, Civ. No. 86-1396-RE (D. ORE.)
(EXCERPTS)

• • •

Plaintiffs allege:

ALLEGATIONS COMMON TO ALL CLAIMS FOR RELIEF

JURISDICTION AND VENUE

1. Count I of each Claim for Relief asserted herein arises under Section 17(a)(1) of the Securities Act of 1933, 15 U.S.C. § 77q(a)(1). Jurisdiction for these Counts is conferred by 15 U.S.C. § 77v. Count II of each Claim for Relief asserted herein arises under Section 10 of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j and 17 C.F.R. 240.10(b)-5. Jurisdiction for these Counts is conferred by 15 U.S.C. § 78aa. Counts IV, V and VI of each Claim for Relief asserted herein arise under the Racketeer Influenced and Corrupt Organizations Act of 1970 ("RICO"), 18 U.S.C. §§ 1962 and 1964. Jurisdiction for these Counts is conferred by 18 U.S.C. §§ 1964 and 1965. Jurisdiction for Counts III and Counts VII through XI of each Claim for Relief asserted herein arise under the principles of pendent jurisdiction.

2. Venue is proper in this district in that the acts alleged herein took place in whole or in part in Oregon, including the sales of the securities described herein, and the plaintiffs' claims arose in this district.

DESCRIPTION OF THE PROGRAMS

3. This action arises out of the packaging, syndication, promotion and sale in Oregon of certain tax shelter limited partnerships known as Duval Associates, LaMar Associates, Mt. Hood Associates, Columbia Associates, Salem Associates, and Troy Associates. As more particularly described herein, these tax shelters involved the purchase and leaseback of certain IBM computer hardware equipment and certain so-called master tapes of computer software programs. Plaintiffs invested in these tax shelters by purchasing limited partnership units in one or more of these partnerships.

4. These tax shelter partnerships were promoted and sold during 1979, 1980, and 1981 to general partners and then to investors as "pre-packaged" programs. The partnerships were identical or virtually identical to each other in several respects, including the following:

a. each partnership was packaged and promoted by the same group of six defendants ("the packagers"), as described more particularly herein;

b. each partnership was comprised of 35 limited partnership "units" and was designed to raise approximately $1 million;

c. each partnership was to enter into identically structured sale and leaseback transactions with respect to the computer equipment and master tape, as described more particularly herein;

d. each partnership was created as a Connecticut limited partnership;

e. the offering memoranda used to promote and sell the partnerships were virtually identical in format and in content;

f. the tax opinions contained in these offering memoranda were virtually identical in format and in content;

g. the equipment appraisals contained in these offering memoranda were virtually identical in format and contained a substantial number of identical or virtually identical phrases;

h. the master tape appraisals contained in these offering memoranda were similar in format and contained a substantial number of identical or virtually identical phrases.

5. These partnerships were also similar to at least twelve other tax shelter limited partnerships packaged and promoted by the packager defendants in Oregon and elsewhere during this same time period, including the limited partnerships known as Euston Associates, Runnels Associates, Lake Associates, Mars Associates, Victoria Associates, Travis Associates, K-T Associates, Bandera Associates, Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum Associates.

6. The tax benefits purportedly to be derived from investing in the limited partnerships described herein were to be achieved through a complex series of purchase, sale and leaseback transactions structured and arranged by the packager defendants. As described in the offering memoranda used to promote and sell the investments, these transactions were to be structured as follows:

a. The equipment transactions

(1) Each partnership was to purchase certain specified IBM computer hardware equipment (the "equipment") from an identified entity. This entity was the immediate seller of the equipment to the partnership and will hereinafter be referred to as the "immediate seller." The partnership was to pay less than 10% of the purchase price of the equipment in cash at closing, and the remainder was to be financed by a 9 year non-recourse note. The equipment was purportedly already subject to a bank debt at the time of this transaction.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the equipment from another identified entity (the "equipment seller") for resale to the partnership.

(3) Simultaneously with purchasing the equipment from the immediate seller, the partnership was to lease the equipment back to the equipment seller under a non-cancellable 9 year lease. The equipment seller would

thereby become a lessee of the equipment from the partnership. This entity will hereinafter be referred to as the "equipment seller/lessee."

(4) At the time of all these transactions, the equipment was represented to be already in place and in use by one or more identified nationally recognized companies (the "user"). The user had purportedly leased the equipment from the equipment seller/lessee before it was sold to the immediate seller for resale to the partnership. This underlying lease (the "user lease") was to expire within 36 to 48 months, at which time the equipment was to be re-leased to another user, if possible. During the pendency of any such subsequent user lease, the partnership was to receive a specified "bonus rental" of approximately 50% of the subsequent user's lease payments.

b. The master tape transactions

(1) In addition to and simultaneously with purchasing the computer equipment, each partnership was to also purchase a master tape for certain specified computer software (the "master tape") from the same immediate seller from whom it had purchased the computer equipment. The master tape was purportedly designed for a specialized function or for use in a specific identified industry, and was purportedly readily marketable for that function or within that industry. The partnership was to pay less than 10% of the purchase price of the master tape in cash at closing, and the remainder was to be financed by a long-term note of approximately 20 years. In addition, each partner in the partnership was to execute a "personal liability agreement" making him or her personally liable for his or her pro-rata share of the partnership's liability on the master tape note.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the master tape from another identified entity (the "master tape seller") for resale to the partnership.

(3) Simultaneously with purchasing the master tape from the immediate seller, the partnership was to lease the master tape back to an identified affiliate of the master tape seller. This entity will hereinafter be referred to as the "master tape lessee."

(4) The master tape lessee was to market and license the master tape to businesses or entities that were in need of the specialized function the software could perform or within the specific industry for which the software was designed. Revenues generated from marketing and licensing the master tape were to be shared with the partnership in the form of certain specified flat and percentage fees paid to the partnership.

7. The offering memoranda issued to promote and sell each of the partnerships and to attract potential investors contained, among other things, the following:

a. a description of the transactions as outlined above;

b. a purportedly independent appraisal of the computer equipment, including an appraisal and valuation of its fair market value, residual value and useful life;

c. a purportedly independent appraisal of the master tape, including an appraisal and valuation of its fair market value and useful life, and a description of potential markets and licensees for the master tape;

d. a tax opinion letter by one of the defendant law firms describing the tax benefits to be derived from investing in the partnership, including eligibility for investment tax credits and for certain deductions based upon depreciation, interest expense, and trade or business expenses.

8. In or around April and/or October, 1984, in connection with the settlement of litigation against them relating to the limited partnerships known as Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum As-

sociates, the packager defendants and defendant Lampf arranged to have all documents and materials relating to or generated in that litigation kept confidential and/or sealed by the court.

DESCRIPTION OF PLAINTIFFS

9. As more particularly described herein, plaintiffs are thirty-nine individuals or entities that invested in one or more of the limited partnerships described herein.

DESCRIPTION OF DEFENDANTS

The Packagers

10. Defendants Leasing Consultants Associates "LCA"), Leasing Consultants, Inc. ("LCI"), William L. McKenna ("McKenna"), Richard A. Heitmeyer ("Heitmeyer"), Richard D. Wellbrock ("Wellbrock") and William B. Ward ("Ward") acted as packagers and promoters of the tax shelter programs sold to plaintiffs, and conceived and arranged for the sale, purchase and lease transactions involved, procured the services of Lampf, Arnheim & McCostis and other defendants, caused the preparation and dissemination of a model offering memoranda, solicited and procured broker/dealers and others to place or sell the limited partnership interests to plaintiffs, and solicited and procured appraisals for the equipment and master tapes.

11. Defendant LCA was at all relevant times a New Jersey general partnership comprised of defendants McKenna, Heitmeyer and Wellbrock.

12. Defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey, and was an affiliate of defendant LCA. Defendants McKenna, Heitmeyer, Wellbrock and Ward were officers and controlling persons of LCI and were, at all relevant times, citizens of the state of New Jersey.

The Immediate Sellers

13. As described above, defendant LCA was at all relevant times a New Jersey general partnership.

14. As described above, defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey.

15. Defendant American Computer Equipment Leasing, Inc. ("ACE") was at all relevant times a corporation doing business in the state of New York.

16. Defendant Computer Systems Consultants, Inc., ("CSC") was at all relevant times a Delaware corporation with its principal office in Ridgewood, New Jersey.

The Equipment Sellers/Lessees

17. Defendant Analysis International Co., Inc. ("Analysis") is or was a corporation with its principal place of business in Charlotte, North Carolina. Defendant Anico Computer Leasing, Inc. ("Anico") is or was a North Carolina corporation and the parent corporation and controlling person of defendant Analysis. Defendants Amato Hernandez ("Hernandez") and John Chandler ("Chandler") are or were officers and controlling persons of Analysis and Anico.

18. Defendant Alanthus Computer Corporation ("Alanthus Computer") and defendant Alanthus Corporation ("Alanthus") are or were Delaware corporations. On information and belief, Alanthus Computer and/or Alanthus are now known as Technology Finance Group. On information and belief, Alanthus Computer and/or Alanthus may have been affiliated with Analysis International Co., Inc.

19. Defendant Rockwood Computer Corporation ("Rockwood") was at all relevant times a corporation with its principal place of business in Elmsford, New York. Defendants Martin S. Karnoff ("Karnoff"), David G.

Marks ("Marks") and John M. Costello ("Costello") are or were officers and controlling persons of Rockwood.

The Master Tape Lessees and Affiliates

20. Defendants Kirby Microprocessors, Inc. ("KMI") and Kirby Computer Systems, Inc. ("Kirby Computer") were at all relevant times corporations doing business in the state of New Jersey. Defendant Robert M. Kirby ("Kirby") is or was the owner and controlling person of KMI and Kirby Computer.

21. Defendants Gordon S. Rosen Associates, Inc. ("Rosen Associates") and Software Systems for Word Processors, Inc. ("SSWPI") were at all relevant times corporations doing business in the state of New York. Defendant Gordon S. Rosen ("Rosen") is or was the owner and controlling person of Rosen Associates and SSWPI.

22. Defendants Robrech Systems, Inc. ("Robrech") and Digitize, Inc. ("Digitize") were at all relevant times corporations doing business in the state of New York.

23. Defendants Buhler Software Services ("Buhler Software") and P-STAT, Inc. ("P-Stat) were at all relevant times corporations doing business in the state of New Jersey. Defendant Roald Buhler ("Buhler") is or was the owner and controlling person of Buhler Software and P-Stat.

24. Defendants ASG Program Products, Inc. ("ASG") and Applications Systems Group, Inc. ("Applications") were at all relevant times corporations doing business in the state of New York. Defendant Martin D. Pine ("Pine") is or was the president and/or controlling person of ASG and Applications.

25. Defendants Start System, Inc. ("Start Systems") and Jeflen Consulting Corporation ("Jeflen") were at all relevant times New York corporations. Defendants Jerrold

Feingold ("J. Feingold") and Leonard Feingold ("L. Feingold") are or were officers and controlling persons of Start Systems and Jeflen.

The Equipment Appraisers

26. Defendant Computer Value Associates ("Computer Value") was at all relevant times a company doing business in the state of New York. Defendant James Cuthbert ("Cuthbert") is or was the president and controlling person of Computer Value.

27. Defendant TexCom Equipment Corporation ("TexCom") and Global Computer Corporation ("Global") were at all relevant times corporations doing business in the state of Texas. Defendant Ronald Johnson ("Johnson") is or was the president, owner, and controlling person of Texcom and Global.

28. Defendant Berlent Industries, Inc. ("Berlent Industries") was at all relevant times a corporation doing business in the state of New York. Defendant Harvey N. Berlent ("Berlent") is or was the president and controlling person of Berlent Industries.

The Master Tape Appraisers

29. Defendant Ward was at all relevant times a citizen of the state of New Jersey.

30. Defendant ConServ International, Inc. ("ConServ") was at all relevant times a corporation doing business in the state of New Jersey. Defendant Robert W. Steinberger ("Steinberger") is or was the president and controlling person of ConServ. Prior to his association with ConServ, Steinberger was vice president of defendant Kirby Computer.

31. Defendant Technical Marketing Services, Inc. ("TMS") was at all relevant times a corporation doing

business in the states of New York and New Jersey. Defendant Leonard F. Turi ("Turi") is or was the president and controlling person of TMS.

32. Defendant Information Industries, Inc. ("Information Industries") was at all relevant times a corporation doing business in the state of New Jersey. Defendant Robert A. Weber ("Weber") is or was an officer and controlling person of Information Industries.

The Attorneys

33. Defendant Lampf, Pleva, Lipkind, Prupis & Petigrow, P.C. ("Lampf") was at all relevant times a professional legal corporation with its principal place of business in the state of New Jersey. Lampf is now known as Lampf, Lipkind, Purpis & Petigrow, P.C.

34. Defendants Anders Arnheim ("Arnheim") and Richard McCostis ("McCostis"), dba the law firm of Arnheim & McCostis, was at all relevant times a New York partnership with its principal place of business in New York, New York. Defendants Robert M. Hurwitz ("Hurwitz") and Noah Schreiber ("Schreiber") were attorneys employed by Arnheim & McCostis and had responsibility for some or all of the professional legal services rendered by Arnheim & McCostis, as described herein. Arnheim, McCostis, Hurwitz, and Schreiber will hereinafter be collectively referred to as "Arnheim & McCostis."

Non-Defendant Co-Conspirator

35. The Lawrence Group was at all material times a consulting firm controlled by defendant William Ward. After the sales of the limited partnership units described herein, The Lawrence Group was engaged by the partnerships, at the suggestion of the packager defendants, purportedly to monitor the status of each of the partnerships' equipment and master tape leases and to make periodic reports to the partnerships describing this status.

FIRST CLAIM FOR RELIEF - DUVAL ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Duval plaintiff.

36. The Duval plaintiff realleges and incorporates by reference paragraphs 1-35, above.

37. The following plaintiff invested in the Duval Associates limited partnership in the amount and on the date indicated below. He shall be referred to herein as the "Duval plaintiff."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Jack R. Stowell	10/79	$ 28,604.00

38. The following defendants participated in the Duval Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Duval defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Duval partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed Duval Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other Duval defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Lampf to: act as general or special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Duval offering memorandum was based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements, on which the Duval partnership agreement and sales and leases agreements were based; and

(7) instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant CSC was immediate seller for the Duval partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Duval equipment") purportedly consisted of an IBM 370/158 Central Processing Unit ("CPU"), an IBM 370/148 CPU, two IBM 370/138 CPU's, and approximately ten pieces of IBM peripheral equipment. The Duval partnership was to pay a total of $1,726,750 for this equipment. The master tape was of a software program known as Kirby Integrated Business Systems ("KIBS"), which was purportedly specially designed for use by home heating oil dealers and readily marketable within that industry. The Duval partnership was to pay a total of $2,000,000 for this master tape. CSC played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that, by purchasing the Duval equipment and the KIBS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Duval partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the

equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. CSC was or should have been aware of its integral role in the Duval partnership and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Alanthus Computer was the equipment seller/lessee for the Duval partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the Duval equipment to the immediate seller, CSC, for resale to the Duval partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the Duval equipment to the end users, which were represented to be General Motors, the Stop & Shop Companies, General Automation Company, and Hills-McCanna Company, and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Alanthus Computer played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that, by selling the Duval equipment to CSC for resale to the Duval partnership, if futher obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that CSC had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Alanthus Computer also added credence to the reasonableness of the end user lease terms described in the Duval offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Alanthus Computer also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to release the equipment at the expiration of the end user leases, in anticipation of a probable IRS objection to the

economic substance of these transactions if the partnership had to seek its own lessees. Alanthus Computer was or should have been aware of its integral role in the Duval partnership and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself.

d. Defendant Kirby Computer was the master tape lessee for the Duval partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the KIBS master tape back from the Duval partnership and was to market and obtain licensees for the use of the master tape. Defendant KMI was an affiliate of Kirby Computer and was the master tape seller for the Duval partnership. As described in paragraph 6b above, in this capacity, it was the entity that sold the KIBS master tape to CSC, the immediate seller, for resale to the Duval partnership. Defendant Kirby was the owner and controlling person of KMI and Kirby Computer. KMI, Kirby Computer, and/or Kirby had purportedly developed the KIBS software program and had purported expertise in marketing the KIBS master tape. On information and belief, Kirby formed Kirby Computer and/or KMI solely for purposes of participating in the Duval partnership. KMI and Kirby played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that, by selling the KIBS master tape to CSC for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if CSC had purchased the tape from an independent third party in an arm's length, negotiated transaction. Kirby Computer and Kirby played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that, by virtue of their purported expertise in the KIBS software program and in the marketing of this software, they appeared capable of successfully exploiting the KIBS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify

the inflated valuation of the tape. KMI, Kirby Computer, and Kirby were or should have been aware of their integral role in the Duval partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Berlent Industries was the equipment appraiser for the Duval partnership. Defendant Berlent was the president and controlling person of Berlent Industries. Defendants Berlent Industries and Berlent prepared a written appraisal of the Duval equipment, on or about October 19, 1979, (hereinafter the "Berlent-Duval appraisal") which appeared in the Duval offering memorandum, and which represented that the fair market value of the Duval equipment was $1.552 million, that the equipment had a useful life in excess of nine years, and that at the end of the nine-year period, its fair market value would be $310,000. Berlent Industries and Berlent played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that the Berlent-Duval appraisal justified the inflated price the partnership was to pay for the Duval equipment and provided the limited partners with "independent" substantiation for the assumptions in the Duval offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user leases, from which the partnership would derive bonus rentals. Berlent Industries and Berlent were or should have been aware that the Berlent-Duval appraisal would be disseminated to prospective investors in Duval Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Berlent-Duval appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market

value, residual value, and useful life of the Duval equipment.

f. In addition to his role as a packager, defendant Ward was also the master tape appraiser for the Duval partnership. In this capacity, he prepared a written appraisal of the KIBS master tape, on or about August 30, 1979, (hereinafter the "Ward-Duval appraisal") which appeared in the Duval offering memorandum, and which represented that the fair market value of the KIBS master tape to be purchased from KMI and leased to Kirby Computer was in excess of $2 million, and that it had a useful life in excess of seven years. This appraisal also represented that the representatives of the Data General Corporation would be actively engaged in marketing the KIBS master tape. This appraisal also represented that the purchase price that the Duval partnership was paying for the KIBS master tape was equal or closer to its appraised fair market value. This appraisal also represented that defendant Ward had met with the management of Kirby Computer and KMI and had reviewed in detail the operation of the KIBS master tape. Ward played an integral and essential role in the fraud perpetrated upon the Duval plaintiff in that the Ward-Duval appraisal justified the inflated price the partnership was to pay for the KIBS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Duval offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the KIBS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least seven years. Ward was or should have been aware that the Ward-Duval appraisal would be disseminated to prospective investors in Duval Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Ward-Duval appraisal in making their investment decisions and to sub-

stantiate, for tax purposes, the fair market value and useful life of the KIBS master tape.

g. Defendant Lampf was the general or special tax counsel for the Duval partnership. In this capacity, Lampf issued a special written tax opinion for the Duval partnership, on or about October, 1979, (hereinafter "the Lampf tax opinion") which appeared in the Duval offering memorandum, and upon which the Duval plaintiff relied in making his investment in Duval Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in Duval Associates. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Duval offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Duval partnership agreement and sales and lease agreements were based.

39. Beginning in or around September, 1979, and continuing to the present, the Duval defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Duval plaintiff in connection with the sale of limited partnership interests in Duval Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Duval computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Duval investors, in addition to income and profits.

40. The Duval plaintiff was induced to invest in Duval Associates by means of an offering memorandum dated September 10, 1979, and a supplemental offering memo-

randum dated October 26, 1979, (hereinafter collectively "the Duval offering memorandum"), which included the Lampf tax opinion, the Berlent-Duval appraisal, and the Ward-Duval appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 38b above, the end users that were purportedly already leasing this equipment, as described in paragraph 38c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 38b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 38e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above.

41. The Duval offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Duval partnership had been, or would be, involved.

42. In connection with the sale of interests in Duval Associates to the Duval plaintiff, the following defendants represented the following:

a. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the KIBS master tape and from the lease income and residual value in the Duval equipment;

b. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that the KIBS master tape program was ready to be marketed in its then-existing format and would readily achieve a significant market share in its target market;

d. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the KIBS master tape program was new and original, and therefore qualified for investment tax credits;

e. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that Kirby Computer and KMI, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the KIBS master tape and thereby generate revenues for the Duval partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

f. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that Ward had met with the management of Kirby Computer and KMI and had become familiar with the operation of the KIBS program;

g. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Berlent Industries and Berlent, in the Berlent-Duval appraisal, represented that the fair market value, residual value, and useful life attributed to the Duval equipment were reasonable and accurate;

h. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, and Ward, in the Ward-Duval appraisal, represented that the fair market

value and useful life attributed to the KIBS master tape were reasonable and accurate;

j. The packagers and Lampf, in the Duval offering memorandum and the Lampf tax opinion, represented that the parties involved in the Duval sale and lease transactions had no conflicts of interest not disclosed in the Duval offering memorandum.

43. These representations were false and misleading in that:

a. The tax benefits and profits promised in the Duval offering memorandum and in the Lampf tax opinion could not be realized by the Duval plaintiff;

b. The actual fair market value, residual value, and useful life of the Duval equipment were substantially less than represented;

c. The actual fair market value and useful life of the KIBS master tape were substantially less than represented;

d. The KIBS master tape was not readily marketable in its target market without substantial modifications in format;

e. On information and belief, the KIBS master tape program was not new or original, and therefore not qualified for investment tax credits;

f. KMI and Kirby Computer did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the KIBS master tape;

g. On information and belief, before issuing the Ward-Duval appraisal, Ward had not met with the management of Kirby Computer and KMI, and had not tested or run the KIBS program and was not familiar with its operation;

h. Ward was a principal of defendant LCI, and therefore had conflicts of interest not disclosed in the Duval offering memorandum.

44. In making the representations described above, the following Duval defendants failed to disclose the following material facts to the Duval plaintiff:

a. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the actual fair market value, residual value, and useful life of the Duval equipment were substantially less than represented in the Duval offering memorandum and in the Berlent-Duval appraisal;

b. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the Duval IBM equipment was likely to become obsolete shortly after it was purchased by the Duval partnership in that IBM frequently announced the introduction of new, better systems that would render the equipment obsolete;

c. The packagers, Lampf, and Ward failed to disclose that the actual fair market value and useful life of the KIBS master tape were substantially less than represented in the Duval offering memorandum and in the Ward-Duval appraisal;

d. The packagers, Lampf, and Ward failed to disclose that the Ward-Duval appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

e. The packagers, Lampf, and Ward failed to disclose that before issuing the Ward-Duval appraisal, Ward had not met with the management of Kirby Computer and KMI, had not tested or run the KIBS program and was not familiar with its contents and operation, and had not adequately researched the marketability of the KIBS master tape;

f. The packagers, Lampf, and Ward failed to disclose that the KIBS master tape was not readily marketable in its target market without substantial modifications in format;

g. The packagers, Lampf, and Ward, failed to disclose that, in order to achieve the market share projected in the Ward-Duval appraisal, the expenses of marketing the KIBS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

h. The packagers and Lampf failed to disclose that Ward was a principal in defendant LCI, and therefore had conflicts of interest not disclosed in the Duval offering memorandum;

i. The packagers, Lampf, and Ward failed to disclose that KMI and Kirby Computer were undercapitalized and without sufficient skill, expertise, and personnel to market and license the KIBS master tape and generate revenues for the partnership; and

j. The packagers and Lampf failed to disclose that the Duval plaintiff would not be entitled to the tax benefits promised in the Duval offering memorandum and the Lampf tax opinion.

45. Defendants Berlent, Berlent Industries, Ward, CSC, Alanthus Computer, KMI, Kirby Computer, and Kirby aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Duval partnership and their actions in furtherance of these roles, as described in paragraphs 38b-f above, were an essential component of the fraud perpetrated on the Duval plaintiff and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Duval plaintiff.

46. Beginning in and around September, 1979, and continuing until the present, the Duval defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and

conspiracy, in or around February, 1980, the packager defendants arranged for The Lawrence Group to be engaged to act as consultant to the partnership and continually assured and represented to the Duval plaintiff, through periodic reports from the Lawrence Group, that lease payments on the Duval equipment lease were current and that diligent efforts were being made to market and obtain licensees for the KIBS master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

47. The Duval plaintiff had no reason to question or doubt the accuracy of any of the representations made by the Duval defendants, as described herein. The Duval plaintiff had no reason to believe that the Duval defendants omitted to state material facts, as described herein. The Duval plaintiff was not aware of the true facts or the facts that the Duval defendants omitted to state. The Duval plaintiff was entitled to and did rely on the Duval defendants' representations, as described herein, and would not have purchased any interests in the Duval limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

48. The Duval plaintiff did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs and described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

49. The Duval plaintiff was duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Duval plaintiff and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 46 above. If the Duval plaintiff or his agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 46 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that he did not have a claim for relief.

50. The Duval plaintiff hereby tenders his limited partnership interest to the Duval defendants.

• • •

COUNT II

(1934 Securities Exchange Act - Section 10(b))

57. The Duval plaintiff realleges and incorporates by reference paragraphs 1-50 above.

58. In connection with the sale of limited partnership interests in Duval Associates, defendants LCA, LCI, McKenna, Wellbrock, Heitmeyer, Ward, and Lampf (the "Duval primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Duval plaintiff; made untrue statements of material fact, as described in paragraphs 42-43 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 44 above, and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Duval plaintiff.

59. The Duval primary violators, and each of them, knew of the falsity of the representations described in paragraph 42 above, or recklessly failed to ascertain the truth of the representations. The Duval primary violators knew of the omissions of material fact described in paragraph 44 above, or recklessly failed to disclose these facts.

60. Defendants CSC, Alanthus Computer, Berlent, Berlent Industries, Ward, KMI, Kirby, and Kirby Computer (the "Duval aiders and abettors") knew that their actions, as described in paragraphs 38b-f, 45 above, furthered and provided substantial assistance to the Duval primary violators in committing a fraud on the Duval plaintiff.

61. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

62. As a result of these acts, the Duval plaintiff is entitled to recover damages equal to all sums paid for his investment, together with interest thereon since the date paid.

* * *

SECOND CLAIM FOR RELIEF - LaMAR ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the LaMar plaintiff.

109. The LaMar plaintiff realleges and incorporates by reference paragraphs 1-35 above.

110. The following plaintiff invested in the LaMar Associates limited partnership in the amount and on the date indicated below. He shall be referred to herein as the "LaMar plaintiff."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Merle Hanset	12/28/79	$ 31,971.00

111. The following defendants participated in the LaMar partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "LaMar defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the LaMar partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed LaMar Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other LaMar defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Lampf to: act as general or special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the LaMar offering memorandum was based, and prepare, print and distribute a model partnership agreement and model sales and lease agreements on which the LaMar partnership agreement and sales and lease agreements were based; and

(7) instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant CSC was the immediate seller for the LaMar partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "LaMar equipment") purportedly consisted of an IBM 370/168 CPU and approximately seven pieces of IBM peripheral equipment. The LaMar partnership was to pay a total of $1,726,750 for this equipment. The master tape was of a software program known as Automated Information Display System ("AID"), which was purportedly specially designed for use by emergency response organizations, such as police and fire departments, and was purportedly readily marketable to such organizations. The LaMar partnership was to pay a total of $2,450,000 for this master tape. CSC played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that, by purchasing the LaMar equipment and the AID master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the LaMar partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. CSC was or should have been aware of its integral role in the LaMar partnership and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Alanthus was the equipment seller/lessee for the LaMar partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the IBM equipment to the immediate seller, CSC, for resale to the LaMar partnership, and then leased the equipment back

from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end user, which was represented to be Associated Hospital Service, Inc., an affiliate of Blue Cross of Wisconsin, and was to re-lease the equipment to a subsequent end user when the existing user lease expired. Alanthus played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that, by selling the LaMar equipment to CSC for resale to the LaMar partnership, if further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that CSC had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Alanthus also added credence to the reasonableness of the end user lease terms described in the LaMar offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Alanthus also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end user lease, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Alanthus was or should have been aware of its integral role in the LaMar partnership and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself.

d. Defendant Digitize was the master tape lessee for the LaMar partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the AID master tape back from the LaMar partnership and was to market and obtain licensees for the use of the master tape. Defendant Robrech was an affiliate of Digitize and was the master tape seller for the LaMar partnership.

As described in paragraph 6b above, in this capacity, it was the entity that sold the AID master tape to CSC, the immediate seller, for resale to the LaMar partnership. Digitize and/or Robrech had purportedly developed the AID software program and had purported expertise in marketing the AID master tape. On information and belief, Digitize and/or Robrech were formed solely for purposes of participating in the LaMar partnership. Robrech played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that, by selling the AID master tape to CSC for resale to the partnership, it made the purchase price of the tape appear reasonable by making it appear as if CSC had purchased the tape from an independent third party in an arm's length, negotiated transaction. Digitize played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that, by virtue of its purported expertise in the AID software program and in the marketing of this software, it appeared capable of succe: sfully exploiting the AID master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Robrech and Digitize were or should have been aware of their integral role in the LaMar partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Berlent Industries was the equipment appraiser for the LaMar partnership. Defendant Berlent was the president and controlling person of Berlent Industries. Defendants Berlent Industries and Berlent prepared a written appraisal of the LaMar equipment, on or about November 6, 1979, (hereinafter "the Berlent-LaMar appraisal") which appeared in the LaMar offering memorandum, and which represented that the current fair market value for the LaMar equipment was $1.85 million, that

it had a useful life in excess of nine years, and that at the end of nine years, it would have a residual value of $420,000. Berlent Industries and Berlent played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that the Berlent-LaMar appraisal justified the inflated price the partnership was to pay for the LaMar equipment and provided the limited partners with "independent" substantiation for the assumptions in the LaMar offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user lease, from which the partnership would derive bonus rentals. Berlent Industries and Berlent were or should have been aware that the Berlent-LaMar appraisal would be disseminated to prospective investors in LaMar Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Berlent-LaMar appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the LaMar equipment.

f. In addition to his role as a packager, defendant Ward was also the master tape appraiser for the LaMar partnership. In this capacity, he prepared a written appraisal of the AID master tape, on or about November 26, 1979, (hereinafter "the Ward-LaMar appraisal") which appeared in the LaMar offering memorandum, and which represented that the fair market value of the AID master tape to be purchased from Robrech and leased to Digitize was in excess of $2.5 million, and that its useful life was at least seven years. This appraisal also represented that the purchase price that the LaMar partnership was paying for the AID master tape was equal or close to this appraisal fair market value. This appraisal also represented that defendant Ward had met with the management, sales,

and technical staff of Robrech and Digitize, had reviewed in detail the contents of the AID master tape, and had conducted independent market research into the target market for the KIBS master tape. Ward played an integral and essential role in the fraud perpetrated upon the LaMar plaintiff in that the Ward-LaMar appraisal justified the inflated price the partnership was to pay for the AID master tape and provided the limited partners with "independent" substantiation for the assumptions in the LaMar offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the AID master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least seven years. Ward was or should have been aware that the Ward-LaMar appraisal would be disseminated to prospective investors in LaMar Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Ward-LaMar appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the AID master tape.

g. Defendant Lampf was the general or special tax counsel for the LaMar partnership. In this capacity, Lampf issued a special written tax opinion for the LaMar partnership, on or about December, 1979, (hereinafter "the Lampf tax opinion") which appeared in the LaMar offering memorandum, and upon which the LaMar plaintiff relied in making his investment in LaMar Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in LaMar Associates. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the LaMar offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the

LaMar partnership agreement and sales and lease agreements were based.

112. Beginning in or around November, 1979, and continuing to the present, the LaMar defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the LaMar plaintiff in connection with the sale of limited partnership interests in LaMar Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the LaMar computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the LaMar investors, in addition to income and profits.

113. The LaMar plaintiff was induced to invest in LaMar Associates by means of an offering memorandum dated November 30, 1979, (hereinafter "the LaMar offering memorandum") which included the Lampf tax opinion, the Berlent-LaMar appraisal, and the Ward-LaMar appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 111b above, the end user that was purportedly already leasing this equipment, as described in paragraph 111c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 111b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 111e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above.

114. In connection with the sale of interests in LaMar Associates to the LaMar plaintiff, the following defendants represented the following:

a. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the AID master tape from the lease income and residual value in the LaMar equipment;

b. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that the AID master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market.

d. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the AID master tape program was new and original, and therefore qualified for investment tax credits;

e. The packager and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that Digitize and Robrech, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the AID master tape and thereby generate revenues for the LaMar partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

f. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that Ward had met with the management and staff of Robrech and Digitize,

had become familiar with the contents of the AID program, and had conducted independent research into the marketability of the AID master tape;

g. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Berlent Industries and Berlent, in the Berlent-LaMar appraisal, represented that the residual value and useful life attributed to the LaMar equipment were reasonable and accurate;

h. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, and Ward, in the Ward-LaMar appraisal, represented that the fair market value and useful life attributed to the AID master tape were reasonable and accurate;

i. The packagers and Lampf, in the LaMar offering memorandum and the Lampf tax opinion, represented that the parties involved in the LaMar sale and lease transactions had no conflicts of interest not disclosed in the LaMar offering memorandum.

115. These representations were false and misleading in that:

a. The tax benefits and profits promised in the LaMar offering memorandum and in the Lampf tax opinion could not be realized by the LaMar plaintiffs;

b. the actual residual value and useful life of the LaMar equipment were substantially less than represented;

c. The actual fair market value and useful life of the AID master tape were substantially less than represented;

d. The AID master tape was not readily marketable in its target market without substantial modifications in format;

e. On information and belief, the AID master tape program was not new or original, and therefore not qualified for investment tax credits;

f. Robrech and Digitize did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the AID master tape;

g. On information and belief, before issuing the Ward-LaMar appraisal, Ward had not met with the management and staff of Robrech and Digitize, had not tested or run the AID program and was not familiar with its contents and operation, and had not independently or thoroughly researched the marketability of the AID master tape;

h. Ward was a principal in defendant LCI, and therefore had conflicts of interest not disclosed in the LaMar offering memorandum.

116. In making the representations described above, the following LaMar defendants failed to disclose the following material facts to the LaMar plaintiff:

a. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the actual residual value and useful life of the LaMar equipment were substantially less than represented in the LaMar offering memorandum and in the Berlent-LaMar appraisal;

b. The packagers, Lampf, Berlent Industries, and Berlent failed to disclose that the LaMar IBM equipment was likely to become obsolete shortly after it was purchased by the LaMar partnership in that IBM frequently announced the introduction of new, better systems that would render the equipment obsolete;

c. The packagers, Lampf, and Ward failed to disclose that the actual fair market value and useful life of the AID master tape program were substantially less than represented in the LaMar offering memorandum and in the Ward-LaMar appraisal;

d. The packagers, Lampf, and Ward failed to disclose that the Ward appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

e. The packagers, Lampf, and Ward failed to disclose that before issuing the Ward-LaMar appraisal, Ward had not met with the management and staff of Robrech and Digitize, had not tested or run the AID program and was not familiar with its contents and operation, and had not independently or adequately researched the marketability of the AID master tape;

f. The packagers, Lampf, and Ward failed to disclose that, in order to achieve the market share projected in the Ward-LaMar appraisal, the expenses of marketing the AID master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

g. The packagers and Lampf failed to disclose that Ward was a principal in defendant LCI and therefore had conflicts of interest not disclosed in the LaMar offering memorandum;

h. The packagers, Lampf, and Ward failed to disclose that Robrech and Digitize were undercapitalized and without sufficient skill, expertise, and personnel to market and license the AID master tape and generate revenues for the partnership;

i. The packagers, Lampf, and Ward failed to disclose that the AID master tape was not readily marketable in its target market with substantial modifications in format; and

j. The packagers and Lampf failed to disclose that the LaMar plaintiff would not be entitled to the tax benefits promised in the LaMar offering memorandum and the Lampf tax opinion.

117. Defendants Berlent, Berlent Industries, Ward, CSC, Alanthus, Robrech, and Digitize aided and abetted in the misrepresentations and omissions alleged above in that their roles in the LaMar partnership and their actions in

furtherance of these roles, as described in paragraphs 111b-f above, were an essential component of the fraud perpetrated on the LaMar plaintiff and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the LaMar plaintiff.

118. Beginning in and around November, 1979, and continuing until the present, the LaMar defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around April, 1980, the packager defendants arranged for The Lawrence Group to be engaged to act as consultant to the partnership and continually assured and represented to the LaMar plaintiff, through periodic reports from The Lawrence Group, that lease payments on the LaMar equipment lease were current and that diligent efforts were being made to market and obtain licensees for the AID master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

119. The LaMar plaintiff had no reason to question or doubt the accuracy of any of the representations made by the LaMar defendants, as described herein. The LaMar plaintiff had no reason to believe that the LaMar defendants omitted to state material facts, as described herein. The LaMar plaintiff was not aware of the true facts or the facts that the LaMar defendants omitted to state. The LaMar plaintiff was entitled to and did rely on the LaMar defendants' representations, as described herein, and would not have purchased any interests in the LaMar limited partnership had the misrepresentations of material

facts not been made or had the omissions of material fact not occurred.

120. The LaMar plaintiff did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

121. The LaMar plaintiff was duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the LaMar plaintiff and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 118 above. If the LaMar plaintiff or his agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 118 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that he did not have a claim for relief.

122. The LaMar plaintiff hereby tenders his limited partnership interest to the LaMar defendants.

• • •

COUNT II

(1934 Securities Exchange Act - Section 10(b))

129. The LaMar plaintiff realleges and incorporates by reference paragraphs 1-35, 110-122, above.

130. In connection with the sale of the limited partnership interests in LaMar Associates, defendants LCA, LCI, McKenna, Wellbrock, Heitmeyer, Ward, and Lampf (the "LaMar primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of

interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the LaMar plaintiff; made untrue statements of material fact, as described in paragraphs 114-115 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading as described in paragraph 116 above, and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the LaMar plaintiff.

131. The LaMar primary violators, and each of them, knew of the falsity of the representations described in paragraph 114 above, or recklessly failed to ascertain the truth of the representations. The LaMar primary violators knew of the omissions of material fact described in paragraph 116 above, or recklessly failed to disclose these facts.

132. Defendants CSC, Alanthus, Berlent, Berlent Industries, Ward, Robrech, and Digitize (the "LaMar aiders and abettors") knew that their actions, as described in paragraphs 111b-f, 117 above, furthered and provided substantial assistance to the LaMar primary violators in committing a fraud on the LaMar plaintiff.

133. These defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

134. As a result of these acts, the LaMar plaintiff is entitled to recover damages equal to all sums paid for his investment, together with interest thereon since the date paid.

* * *

THIRD CLAIM FOR RELIEF -
MT. HOOD ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Mt. Hood plaintiffs.

190. The Mt. Hood plaintiffs reallege and incorporate by reference paragraphs 1-35 above.

191. The following plaintiffs invested in the Mt. Hood Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Mt. Hood plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Bitar Bros.	9/80	$ 30,805.00
Loren E. Parks	9/22/80	184,830.00
David E. Howard, Sr.	9/80	30,805,00
Shirley S. Matchette	9/80	30,805.00
R & D Investment Co.	9/16/80	30,805.00
Willis Sprattling	9/23/80	30,805.00
Verne Adams	9/80	30,805.00
Claude Abouchedid	9/17/80	30,805.00
James H. Hambleton	9/80	30,805.00
Mark S. Kochevar	9/19/80	30,805.00
William R. Stewart	9/80	30,805.00

192. The following defendants participated in the Mt. Hood Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Mt. Hood defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Mt. Hood partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed Mt. Hood Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other Mt. Hood defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Mt. Hood offering memorandum was based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements on which the Mt. Hood partnership agreement and sales and lease agreements were based; and

(7) instructing defendant Lampf w th respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. Defendant ACE was the immediate seller for the Mt. Hood partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Mt. Hood equipment") purportedly consisted of an IBM 370/158 CPU and approximately 26 pieces of IBM peripheral equipment. The Mt. Hood partnership was to pay a total of $1,750,000 for this equipment. The master tape was of a software program known as the P-Stat Preprocessor Program ("P-STAT"), which was purportedly specially designed to allow computer programs written in the Fortran language to be economically adapted for use on most makes of computers, and was purportedly readily marketable for that function to major companies and other

businesses using several different makes of computers. The Mt. Hood partnership was to pay a total of $2,300,000 for this master tape. ACE played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by purchasing the Mt. Hood equipment and the P-STAT master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Mt. Hood partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. ACE was or should have been aware of its integral role in the Mt. Hood partnership and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Analysis was the equipment seller/lessee for the Mt. Hood Associates partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the IBM equipment to the immediate seller, ACE, for release to the Mt. Hood partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the Mt. Hood equipment to the end user, which was represented to be the Russell Corporation, and was to re-lease the equipment to a subsequent end user when the existing user lease expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by selling the Mt. Hood equipment to ACE for resale to the Mt. Hood partnership, it further obscured the original purchase price of the equipment, provided part of the jus-

tification for the inflated price the partnership was to pay for the equipment, and provided the illusion that ACE had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end user lease terms described in the Mt. Hood offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to release the equipment at the expiration of the end user lease, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Mt. Hood partnership and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself.

d. Defendant P-Stat was the master tape lessee for the Mt. Hood partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the P-STAT master tape back from the Mt. Hood partnership and was to market and obtain licensees for the use of the master tape. Defendant Buhler Software was an affiliate of P-Stat Software and was the master tape seller for the Mt. Hood partnership. As described in paragraph 6b above, in this capacity, it was the entity that sold the P-STAT master tape to ACE, the immediate seller, for resale to the Mt. Hood partnership. Defendant Buhler was the owner and controlling person of Buhler Software and P-Stat. Buhler Software, P-Stat and/or Buhler had purportedly developed the P-STAT software program and had purported expertise in marketing the P-STAT master tape. On information and belief, Buhler formed Buhler Software and/or P-Stat solely for purposes of participating in the Mt. Hood partnership. Buhler Software and Buhler played

an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by selling the P-STAT master tape to ACE for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if ACE had purchased the tape from an independent third party in an arm's length, negotiated transaction. P-Stat and Buhler played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that, by virtue of their purported expertise in the P-STAT software program and in the marketing of this software, they appeared capable of successfully exploiting the P-STAT master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Buhler Software, P-Stat, and Buhler were or should have been aware of their integral role in the Mt. Hood partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Texcom was the equipment appraiser for the Mt. Hood partnership. Defendant Johnson was the president, owner, and controlling person of Texcom. Defendants Texcom and Johnson prepared a written appraisal of the Mt. Hood equipment, on or about July 31, 1980, (hereinafter "the Texcom appraisal") which appeared in the Mt. Hood offering memorandum, and which represented that the Mt. Hood equipment had a fair market value of $1.8 million, had a useful life in excess of nine years, and would have a residual value at the end of nine years in excess of $360,000. Texcom and Johnson played an integral and essential role in the fraud perpetrated upon the Mt. Hood plaintiffs in that the Texcom appraisal justified the inflated price the partnership was to pay for the Mt. Hood equipment and provided the limited partners with "independent" substantiation for the assumptions in

the Mt. Hood offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user lease, from which the partnership would derive bonus rentals. Texcom and Johnson were or should have been aware that the Texcom appraisal would be disseminated to prospective investors in Mt. Hood Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Texcom appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Mt. Hood equipment.

f. Defendant ConServ was the master tape appraiser for the Mt. Hood partnership. Defendant Steinberger was the president and controlling person of ConServ. Defendants ConServ and Steinberger prepared a written appraisal of the P-STAT master tape, on or about August 1, 1980, (hereinafter "the ConServ appraisal") which appeared in the Mt. Hood offering memorandum, and which represented that the fair market value of the P-STAT master tape to be purchased from Buhler Software and leased to P-Stat was in excess of $2.4 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Mt. Hood partnership was paying for the P-STAT master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Steinberger had met with the management and technical staff of Buhler Software and P-Stat, had examined in detail the contents of the P-STAT master tape, and had discussed with Buhler Software and P-Stat the underlying objective of the P-STAT program, its current development and operational status, and the market segment that could benefit from licensing the P-STAT master tape. ConServ and Steinberger played an integral and essential role in the fraud

perpetrated upon the Mt. Hood plaintiffs in that the ConServ appraisal justified the inflated price the partnership was to pay for the P-STAT master tape and provided the limited partners with "independent" substantiation for the assumptions in the Mt. Hood offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the P-STAT master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. ConServ and Steinberger were or should have been aware that the ConServ appraisal would be disseminated to prospective investors in Mt. Hood Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the ConServ appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the P-STAT master tape.

g. Defendant Lampf was the special tax counsel for the Mt. Hood partnership. In this capacity, Lampf issued a special written tax opinion for the Mt. Hood partnership, on or about October, 1980, (hereinafter "the Lampf tax opinion") which appeared in the Mt. Hood offering memorandum, and upon which the Mt. Hood plaintiffs relied in making their investment in Mt. Hood Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in Mt. Hood Associates. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Mt. Hood offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Mt. Hood Associates partnership agreement and sales and lease agreements were based.

193. Beginning in or around August, 1980, and continuing to the present, the Mt. Hood defendants, in concert

and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Mt. Hood plaintiffs in connection with the sale of limited partnership interests in Mt. Hood Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Mt. Hood computer equipment and master tape described above. This program was purportedly designed to general substantial tax benefits to the Mt. Hood investors, in addition to income and profits.

194. The Mt. Hood plaintiffs were induced to invest in Mt. Hood Associates by means of an offering memorandum dated August 1, 1980 (hereinafter "the Mt. Hood offering memorandum"), which included the Lampf tax opinion, the Texcom appraisal, and the ConServ appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 192b above, the end user that was purportedly already leasing this equipment, as described in paragraph 192c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 192b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 192e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Steinberger, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants in the Mt. Hood partnership had been, or would be, involved.

195. In connection with the sale of interests in Mt. Hood Associates to the Mt. Hood plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the P-STAT master tape and from the lease income and residual value in the Mt. Hood equipment;

b. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the Mt. Hood equipment existed, was specifically identified, and was already under lease to the Russell Corporation on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that the P-STAT master tape program was ready to market in its then-existing format and would readily achieve a significant market share in its target market;

e. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, represented that the P-STAT master tape program was new and original, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that P-Stat and Buhler Software, the master tape lessee

and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the P-STAT master tape and thereby generate revenues for the Mt. Hood partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the Con-Serv appraisal, represented that Steinberger had met with the management and staff of Buhler Software and P-Stat, and had become familiar with the contents and operation of the P-STAT program and the marketing potential of the P-STAT master tape;

h. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and Texcom and Johnson, in the Texcom appraisal, represented that the fair market value, residual value, and useful life attributed to the Mt. Hood equipment were reasonable and accurate;

i. The packagers and Lampf, in the Mt. Hood offering memorandum and the Lampf tax opinion, and ConServ and Steinberger, in the ConServ appraisal, represented that the fair market value and useful life attributed to the P-STAT master tape were reasonable and accurate.

196. These representations were false and misleading in that:

a. The IBM computer equipment described in the Mt. Hood offering memorandum did not exist or was not under lease to the end user, the Russell Corporation, as represented;

b. The tax benefits and profits promised in the Mt. Hood offering memorandum and in the Lampf tax opinion could not be realized by the Mt. Hood plaintiffs;

c. The actual fair market value, residual value, and useful life of the Mt. Hood equipment were substantially less than represented;

d. The actual fair market value and useful life of the P-STAT master tape were substantially less than represented;

e. The P-STAT master tape was not readily marketable in its target market without substantial modifications in format;

f. On information and belief, the P-STAT master tape program was not new or original, and therefore not qualified for investment tax credits;

g. Buhler Software and P-Stat did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the P-STAT master tape;

h. On information and belief, before issuing the ConServ appraisal, Steinberger had not met with the management and staff of Buhler Software and P-Stat, had not tested or run the P-STAT program and was not familiar with its contents and operation, and had not thoroughly investigated the marketability of the P-STAT master tape.

197. In making the representations described above, the following Mt. Hood defendants failed to disclose the following material facts to the Mt. Hood plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Mt. Hood offering memorandum was not in fact the equipment owned by ACE or Analysis and purchased by the partnership;

b. The packagers and Lampf failed to disclose that the IBM equipment described in the Mt. Hood offering memorandum was not currently under lease to the Russell Corporation, the purported end user;

c. The packagers, Lampf, Texcom, and Johnson failed to disclose that the actual fair market value, residual value,

and useful life of the Mt. Hood equipment were substantially less than represented in the Mt. Hood offering memorandum and in the Texcom appraisal;

d. The packagers, Lampf, Texcom, and Johnson failed to disclose that they had not performed any investigation to examine the equipment or to verify its existence and condition;

e. The packagers, Lampf, Texcom, and Johnson failed to disclose that the Mt. Hood IBM equipment was essentially obsolete at the time it was purchased by the Mt. Hood partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the actual fair market value and useful life of the P-STAT master tape were substantially less than represented in the Mt. Hood offering memorandum and in the ConServ appraisal;

g. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the ConServ appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Lampf, ConServ, and Steinberger failed to disclose that before issuing the ConServ appraisal, Steinberger had not met with the management and staff of Buhler Software and P-Stat, had not tested or run the P-STAT program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the P-STAT master tape;

i. The packagers, Lampf, ConServ, and Steinberger failed to disclose that, in order to achieve the market share projected in the ConServ appraisal, the expenses of marketing the P-STAT master tape would be enormous, and that these expenses would need to be paid out of any

gross revenues received from licensing the master tape before any profit could be returned to the partnership;

j. The packagers, Lampf, ConServ, and Steinberger failed to disclose that Buhler Software and P-Stat were under-capitalized and without sufficient skill, expertise, and personnel to market and license the P-STAT master tape and generate revenues for the partnership;

k. The packagers, Lampf, ConServ, and Steinberger failed to disclose that the P-STAT master tape was not readily marketable in its target market without substantial modifications in format; and

l. The packagers and Lampf failed to disclose that the Mt. Hood plaintiffs would not be entitled to the tax benefits promised in the Mt. Hood offering memorandum and the Lampf tax opinion.

198. Defendants Johnson, Texcom, ConServ, Steinberger, ACE, Analysis, Hernandez, Chandler, Anico, Buhler Software, P-Stat, and Buhler aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Mt. Hood partnership and their actions in furtherance of these roles, as described in paragraphs 192b-f above, were an essential component of the fraud perpetrated on the Mt. Hood plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Mt. Hood plaintiffs.

199. Beginning in and around August, 1980, and continuing until the present, the Mt. Hood defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around February, 1981, the packager defendants arranged for Mr. Steinberger to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Mt.

Hood plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Mt. Hood equipment lease were current and that diligent efforts were being made to market and obtain licensees for the P-STAT master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they attributed to unanticipated events or market trends.

200. In or around August, 1982, the Mt. Hood partnership sought to rescind its purchase of the P-STAT master tape because efforts to obtain licensees for the master tape had not been as successful as hoped. In or around October, 1982, in connection with this rescission and in an effort to mislead the Mt. Hood limited partners and to conceal the fraud alleged herein, the packagers and/or their attorney, Michael Dell, represented to and assured the attorneys for the Mt. Hood partnership, Burt & Hagen, P.C., that the marketing difficulties encountered by the master tape marketers were the result of unforeseen circumstances and that the packagers stood behind the representations in the Mt. Hood offering memorandum. In a further effort to lull the Mt. Hood limited partners and to conceal the fraud alleged herein, the packagers arranged for the seller of the P-STAT master tape to repurchase the tape at no loss to the partnership, and procured a substitute real estate investment for the partnership.

201. The Mt. Hood plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Mt. Hood defendants, as decribed herein. The Mt. Hood plaintiffs had no reason to believe that the Mt. Hood defendants omitted to state material facts, as described herein. The Mt. Hood plaintiffs were not aware of the true facts or the facts that the Mt. Hood defendants omitted to state. The Mt. Hood plaintiffs were entitled to and did

rely on the Mt. Hood defendants' representations, as described herein, and would not have purchased any interests in the Mt. Hood limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

202. The Mt. Hood plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

203. The Mt. Hood plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Mt. Hood plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 199-200 above. If the Mt. Hood plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 199-200 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

204. The Mt. Hood plaintiffs hereby tender their limited partnership interests to the Mt. Hood defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b))

211. The Mt. Hood plaintiffs reallege and incorporate by reference paragraphs 1-35, 191-204, above.

212. In connection with the sale of the limited partnership interests in Mt. Hood Associates, defendants LCI,

LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf (the "Mt. Hood primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Mt. Hood plaintiffs; untrue statements of material fact, as described in paragraphs 195-196 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 197 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Mt. Hood plaintiffs.

213. The Mt. Hood primary violators, and each of them, knew of the falsity of the representations described in paragraph 195 above, or recklessly failed to ascertain the truth of the representations. The Mt. Hood primary violators knew of the omissions of material fact described in paragraph 197 above, or recklessly failed to disclose these facts.

214. Defendants ACE, Analysis, Hernandez, Chandler, Anico, Johnson, TexCom, Buhler, Buhler Software, P-Stat, ConServ, and Steinberger, (the "Mt. Hood aiders and abettors") knew that their actions, as described in paragraphs 192b-f, 198 above, furthered and provided substantial assistance to the primary violaters in committing a fraud on the Mt. Hood plaintiffs.

215. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

216. As a result of these acts, the Mt. Hood plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

FOURTH CLAIM FOR RELIEF - COLUMBIA ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Columbia plaintiffs.

271. The Columbia plaintiffs reallege and incorporate by reference paragraphs 1-35 above.

272. The following plaintiffs invested in the Columbia Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Columbia plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Merle Hanset	12/80	$26,805.00
Gordon S. Gleason	12/80	26,805.00
Carl L.J. Golder	12/80	26,805.00
Lee C. Golder	12/80	26,805.00

273. The following defendants participated in the Columbia Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Columbia defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Columbia partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed Columbia Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other Columbia defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Columbia offering memorandum was based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements on which the Columbia partnership agreement and sales and lease agreements were based; and

(7) instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, defendant LCI was also the immediate seller for the Columbia partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Columbia equipment") purportedly consisted of two IBM 370/158 CPU's, an IBM Printing Subsystem, and approximately thirteen pieces of IBM peripheral equipment. The Columbia partnership was to pay a total of $1,450,000 for this equipment. The master tape was of a software program known as Office Automation System ("OAS"), which was purportedly specially designed to perform basic accounting functions, such as payroll and receivables, on Xerox and Wang word processing units, and was purportedly readily marketable to businesses having those makes of word processing units. The Columbia partnership was to pay a total of $1,950,000 for this master tape. Defendants McKenna, Heitmeyer, Wellbrock, and Ward were principals and controlling persons of defendant LCI. LCI played

an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by purchasing the Columbia equipment and the OAS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Columbia partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCI was or should have been aware of its integral role in the Columbia partnership and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Analysis was the equipment seller/lessee for the Columbia partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the Columbia equipment to the immediate seller, LCI, for resale to the Columbia partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end users, which were represented to be W.R. Grace & Company, Westinghouse Electric Corporation, and Spring Mills, Inc., and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by selling the Columbia equipment to LCI for resale to the Columbia partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCI

had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end user lease terms described in the Columbia offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Columbia partnership and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself.

d. Defendant SSWPI was the master tape lessee for the Columbia partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the OAS master tape back from the Columbia partnership and was to market and obtain licensees for the use of the master tape. Defendant Rosen Associates was an affiliate of SSWPI and was the master tape seller for the Columbia partnership. As described in paragraph 6b above, in this capacity, it was the entity that sold the OAS master tape to LCI, the immediate seller, for resale to the Columbia partnership. Defendant Rosen was the owner and controlling person of Rosen Associates and SSWPI. Rosen Associates, SSWPI, and/or Rosen had purportedly developed the OAS software program and had purported expertise in marketing the OAS master tape. On information and belief, Rosen formed Rosen Associates and/or SSWPI solely for purposes of participating in the Columbia partnership. Rosen Associates and Rosen played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by selling the OAS master tape

to LCI for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCI had purchased the tape from an independent third party in an arm's length, negotiated transaction. SSWPI and Rosen played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that, by virtue of their purported expertise in the OAS software program and in the marketing of this software, they appeared capable of successfully exploiting the OAS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Rosen Associates, SSWPI, and Rosen were or should have been aware of their integral role in the Columbia partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Computer Value was the equipment appraiser for the Columbia partnership. Defendant Cuthbert was the president and controlling person of Computer Value. Defendants Computer Value and Cuthbert prepared a written appraisal of the Columbia equipment, on or about September 29, 1980 (hereinafter "the Cuthbert-Columbia appraisal") which appeared in the Columbia offering memorandum, and which represented that the Columbia equipment had a fair market value of 1.5 million, a useful life in excess of nine years, and a residual value at the end of nine years in excess of $300,000. Computer Value and Cuthbert played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that the Cuthbert-Columbia appraisal justified the inflated price the partnership was to pay for the Columbia equipment and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was

reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user leases, from which the partnership would derive bonus rentals. Computer Value and Cuthbert were or should have been aware that the Cuthbert-Columbia appraisal would be disseminated to prospective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Cuthbert-Columbia appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Columbia equipment.

f. Defendant TMS was the master tape appraiser for the Columbia partnership. Defendant Turi was the president and controlling person of TMS. Defendants TMS and Turi prepared a written appraisal of the OAS master tape, on or about October 31, 1980, (hereinafter "the TMS-Columbia appraisal") which appeared in the Columbia offering memorandum, and which represented that the fair market value of the OAS master tape to be purchased from Rosen Associates and leased to SSWPI was in excess of $3.4 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Columbia partnership was paying for the OAS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Turi had met with the management and technical staff of Rosen Associates and SSWPI, had examined in detail the contents of the OAS master tape, and had discussed with Rosen Associates and SSWPI the underlying objectives of the OAS program, its current development and operational status, the marketing plans contemplated by SSWPI, and the market segments that could benefit from licensing the OAS master tape. TMS and Turi played an integral and essential role in the fraud perpetrated upon the Columbia plaintiffs in that the TMS-Columbia appraisal justified the inflated price the partnership was to pay for the OAS

master tape and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the OAS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. TMS and Turi were or should have been aware that the TMS-Columbia appraisal would be disseminated to prospective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the TMS-Columbia appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the OAS master tape.

g. Defendant Lampf was the special tax counsel for the Columbia partnership. In this capacity, Lampf issued a special written tax opinion for the Columbia partnership, on or about October, 1980, (hereinafter "the Lampf tax opinion") which appeared in the Columbia offering memorandum, and upon which the Columbia plaintiffs relied in making their investment in Columbia Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in Columbia Associates. Lampf was paid at least $20,000 for preparing this tax option. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Columbia offering memorandum was based. Lampf also prepared, printd, and distributed a model partnership agreement and model sales and lease agreements, on which the Columbia partnership agreement and sale lease agreements were based.

274. Beginning in or around November, 1980, and continuing to the present, the Columbia defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Columbia plaintiffs in connection with the sale of limited

partnership interests in Columbia Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and lease-back the Columbia computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Columbia investors, in addition to income and profits.

275. The Columbia plaintiffs were induced to invest in Columbia Associates by means of an offering memorandum dated November 14, 1980, and a supplemental offering memorandum dated December 29, 1980 (hereinafter collectively "the Columbia offering memorandum"), which included the Lampf tax opinion, the Cuthbert-Columbia appraisal, and the TMS-Columbia appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 273b above, the end users that were purportedly already leasing this equipment, as described in paragraph 273c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 273b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 273e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Turi, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

276. The Columbia offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Columbia partnership had been, or

would be, involved. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants in the Columbia partnership had been, or would be, involved.

277. In connection with the sale of interests in Columbia Associates to the Columbia plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the OAS master tape and from the lease income and residual value in the Columbia equipment;

b. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the Columbia equipment existed, was specifically identified, and was already under lease to W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc. on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the OAS master tape program was ready to be marketed in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that

the OAS master tape program was new and original, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that SSWPI and Rosen Associates, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the OAS master tape and thereby generate revenues for the Columbia partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership.

g. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that Turi had met with the management and staff of Rosen Associates and SSWPI, and had become familiar with the contents and operation of the OAS program and the marketing potential of the OAS master tape;

h. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the fair market value, residual value, and useful life attributed to the Columbia equipment were reasonable and accurate;

i. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the fair market value and useful life attributed to the OAS master tape were reasonable and accurate.

278. These representations were false and misleading in that:

a. The IBM computer equipment described in the Columbia offering memorandum did not exist or was not

under lease to the end users, W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., as represented;

b. The tax benefits and profits promised in the Columbia offering memorandum and in the Lampf tax opinion could not be realized by the Columbia plaintiffs;

c. The actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented;

d. The actual fair market value and useful life of OAS master tape were substantially less than represented;

e. The OAS master tape was not readily marketable in its target market without substantial modifications informat;

f. On information and belief, the OAS master tape program was not new or original, and therefore not qualified for investment tax credits;

g. Rosen Associates and SSWPI did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the OAS master tape;

h. On information and belief, before issuing the TMS-Columbia apraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the OAS master tape.

279. In making the representations described above, the following Columbia defendants failed to disclose the following material facts to the Columbia plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Columbia offering memorandum was not in fact the equipment owned by LCI or Analysis and purchased by the partnership;

b. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the IBM equipment described

in the Columbia offering memorandum was not currently under lease to W.R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., the purported end users;

c. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented in the Columbia offering memorandum and in the Cuthbert-Columbia appraisal;

d. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that they had not performed any investigation to examine the Columbia equipment or to verify its existence and condition;

e. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the Columbia IBM equipment was essentially obsolete at the time it was purchased by the Columbia partnership in that IBM had already announced the introduction of new, better systems that wou.d render the equipment obsolete;

f. The packagers, Lampf, TMS, and Turi failed to disclose that the actual fair market value and useful life of the OAS master tape were substantially less than represented in the Columbia offering memorandum and in the TMS-Columbia appraisal;

g. The packagers, Lampf, TMS, and Turi failed to disclose that the TMS-Columbia appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Lampf, TMS, and Turi failed to disclose that before issuing the TMS-Columbia appraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the OAS master tape;

i. The packagers, Lampf, TMS, and Turi failed to disclose that, in order to achieve the market share projected in the TMS-Columbia appraisal, the expenses of marketing the OAS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

j. The packagers, Lampf, TMS, and Turi failed to disclose that Rosen Associates and SSWPI were undercapitalized and without sufficient skill, expertise, and personnel to market and license the OAS master tape and generate revenues for the partnership;

k. The packagers, Lampf, TMS, and Turi failed to disclose that the OAS master tape was not readily marketable in its target market without substantial modifications in format; and

l. The packagers and Lampf failed to disclose that the Columbia plaintiffs would not be entitled to the tax benefits promised in the Columbia offering memorandum and the Lampf tax opinion.

280. Defendants Cuthbert, Computer Value, TMS, Turi, LCI, Analysis, Hernandez, Chandler, Anico, Rosen Associates, SSWPI, and Rosen aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Columbia partnership and their actions in furtherance of these roles, as described in paragraphs 273b-f above, were an essential component of the fraud perpetrated on the Columbia plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf, in committing a fraud on the Columbia plaintiffs.

281. Beginning in and around November, 1980, and continuing until the present, the Columbia defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and

omissions described herein. In furtherance of this scheme and conspiracy, in or around April, 1981, the packager defendants arranged for Mr. Turi be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Columbia plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Columbia equipment lease were current and that diligent efforts were being made to market and obtain licensees for the OAS master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

282. The Columbia plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Columbia defendants, as described herein. The Columbia plaintiffs had no reason to believe that the Columbia defendants omitted to state material facts, as described herein. The Columbia plaintiffs were not aware of the true facts or the facts that the Columbia defendants omitted to state. The Columbia plaintiffs were entitled to and did rely on the Columbia defendants' representations, as described herein, and would not have purchased any interests in the Columbia limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

283. The Columbia plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

284. The Columbia plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Columbia plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 281 above. If the Columbia plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 281 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

285. The Columbia plaintiffs hereby tender their limited partnership interests to the Columbia defendants.

• • •

COUNT II

(1934 Securities Exchange Act - Section 10(b))

292. The Columbia plaintiffs reallege and incorporate by reference paragraphs 1-35, 272-285, above.

293. In connection with the sale of the limited partnership interests in Columbia Associates, defendants LCI, LCA, McKenna, Wellbrock, Ward, and Lampf (the "Columbia primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Columbia plaintiffs; made untrue statements of material fact, as described in paragraphs 277-278 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 279 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Columbia plaintiffs.

294. The Columbia primary violators, and each of them, knew of the falsity of the representations described in paragraph 277 above, or recklessly failed to ascertain the truth of the representations. The Columbia primary violators knew of the omissions of material fact described in paragraph 279 above, or recklessly failed to disclose these facts.

295. Defendants Analysis, Hernandez, Chandler, Anico, LCI, Computer Value, Cuthbert, Rosen Associates, SSWPI, Rosen, TMS, and Turi (the Columbia "aiders and abettors") knew that their actions, as described in paragraphs 273b-f, 280 above, furthered and provided substantial assistance to the Columbia primary violators in committing a fraud on the Columbia plaintiffs.

296. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

297. As a result of these acts, the Columbia plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

* * *

FIFTH CLAIM FOR RELIEF - SALEM ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Salem plaintiffs.

352. The Salem plaintiffs reallege and incorporate by reference paragraphs 1-35 above.

353. The following plaintiffs invested in the Salem Associates limited partnership in the amounts and on the dates indicated below. They shall be referred to herein as the "Salem plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
Donald G. Brauer	12/23/80	$25,227.00
Beverly S. Knoblock	12/80	25,227.00
Richard H. Schweiger	12/22/80	25,227.00
Frank L. Whittaker	12/24/80	25,227.00
H. Wayne Thompson	12/80	25,227.00

354. The following defendants participated in the Salem Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Salem defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Salem partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed Salem Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other Salem defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Salem offering memorandum was based, and prepare, print, and distribute a model partnership agreement and model sales and lease agreements, on which the Salem

partnership agreement and sales and lease agreements were based; and,

(7) instructing defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, defendant LCI was also the immediate seller for the Salem partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Salem equipment") purportedly consisted of three IBM 3800 Printing Subsystems. The Salem partnership was to pay a total of $1,115,000 for this equipment. The master tape was of a software program known as Insurance Brokers and Agents System ("IBAS"), which was purportedly specially designed for use by insurance offices to perform routine administrative and accounting functions, and was purportedly readily marketable within that industry. The Salem partnership was to pay a total of $1,900,000 for this master tape. Defendants McKenna, Heitmeyer, Wellbrock, and Ward were principals and controlling persons of defendant LCI. LCI played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by purchasing the Salem equipment and the IBAS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Salem partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCI was or should have been aware of its integral role in the Salem partnership and of the lack of economic substance in these transactions in that it both bought and sold the

equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Analysis was the equipment seller/lessee for the Salem partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the IBM equipment to the immediate seller, LCI, for resale to the Salem partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end user, which was represented to be the Coleman Company, and was to re-lease the equipment to a subsequent end user when the existing user lease expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by selling the Salem equipment to LCI for resale to the Salem partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCI had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end user lease terms described in the Salem offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end user lease, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Salem partnership and of the lack of economic substance in these transactions in that it made a substantial profit

as a result of these transactions with little or no risk to itself.

d. Defendant Applications was the master tape lessee for the Salem partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the IBAS master tape back from the Salem partnership and was to market and obtain licensees for the use of the master tape. Defendant ASG was an affiliate of Applications and was the master tape seller for the Salem partnership. As described in paragraph 6b above, in this capacity, it was the entity that sold the IBAS master tape to LCI, the immediate seller, for resale to the Salem partnership. Defendant Pine was the president and controlling person of ASG and Applications. ASG, Applications, and/or Pine had purportedly developed the IBAS software program and had purported expertise in marketing the IBAS master tape. On information and belief, Pine formed ASG and/or Applications solely for purposes of participating in the Salem partnership. ASG and Pine played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by selling the IBAS master tape to LCI for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCI had purchased the tape from an independent third party in an arm's length, negotiated transaction. Applications and Pine played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that, by virtue of their purported expertise in the IBAS software program and in the marketing of this software, they appeared capable of successfully exploiting the IBAS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. ASG, Applications, and Pine were or should have been aware of their integral role in the Salem partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result

of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Global was the equipment appraiser for the Salem partnership. Defendant Johnson was the president, owner, and controlling person of Global. Defendants Global and Johnson prepared a written appraisal of the Salem equipment, on or about November 24, 1980, (hereinafter "the Global appraisal") which appeared in the Salem offering memorandum, and which represented that the Salem equipment had a fair market value in excess of $1.115 million, that it had a useful life of nine years, and that at the end of nine years, it would have a residual value of $225,000. Global and Johnson played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that the Global appraisal justified the inflated price the partnership was to pay for the Salem equipment and provided the limited partners with "independent" substantiation for the assumptions in the Salem offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user lease, from which the partnership would derive bonus rentals. Global and Johnson were or should have been aware that the Global appraisal would be disseminated to prospective investors in Salem Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Global appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Salem equipment.

f. Defendant TMS was the master tape appraiser for the Salem partnership. Defendant Turi was the president and controlling person of TMS. Defendants TMS and Turi prepared a written appraisal of the IBAS master tape, on or about November 26, 1980, (hereinafter "the TMS-Salem

appraisal") which appeared in the Salem offering memorandum, and which represented that the IBAS master tape to be purchased from ASG and leased to Applications had a fair market value in excess of $2,190,000, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Salem partnership was paying for the IBAS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Turi had met with the management and technical staff of ASG and Applications, had examined in detail the contents of the IBAS master tape, and had discussed with ASG and Applications the underlying objectives of the IBAS program, its current development and operational status, the marketing plans contemplated by Applications, and the market segments that could benefit from licensing the IBAS master tape. TMS and Turi played an integral and essential role in the fraud perpetrated upon the Salem plaintiffs in that the TMS-Salem appraisal justified the inflated price the partnership was to pay for the IBAS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Salem offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the IBAS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. TMS and Turi were or should have been aware that the TMS-Salem appraisal would be disseminated to prospective investors in Salem Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the TMS-Salem appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the IBAS master tape.

g. Defendant Lampf was the special tax counsel for the Salem partnership. In this capacity, Lampf issued a special written tax opinion for the Salem partnership, on

or about December, 1980, (hereinafter "the Lampf tax opinion") which appeared in the Salem offering memorandum, and upon which the Salem plaintiffs relied in making their investment in Salem Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in Salem Associates. Lampf was paid at least $20,000 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Salem offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model partnership sales and lease agreements, on which the Salem Associates partnership agreement and sales and lease agreements were based.

355. Beginning in or around December, 1980, and continuing to the present, the Salem defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Salem plaintiffs in connection with the sale of limited partnership interests in Salem Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Salem computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Salem investors, in addition to income and profits.

356. The Salem plaintiffs were induced to invest in Salem Associates by means of an offering memorandum dated December 4, 1980 (hereinafter "the Salem offering memorandum"), which included the Lampf tax opinion, the Global appraisal, and the TMS-Salem appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 354b above, the end user that was purportedly already leasing this

equipment, as described in paragraph 354c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 354b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 354e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Turi, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

357. The Salem offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Salem partnership had been, or would be, involved. This offering memorandum also stated that defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in which some or all of the participants the Salem partnership had been, or would be, involved.

358. In connection with the sale of interests in Salem Associates to the Salem plaintiffs, the following defendants represented the following:

a. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the IBAS master tape and from the lease income and residual value in the Salem equipment;

b. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the Lampf tax opinion supported the investors' entitlement

to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and Global and Johnson, in the Global appraisal, represented that the Salem equipment existed, was specifically identified, and was already under lease to the Coleman Company on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that the IBAS master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, represented that the IBAS master tape program was new and original, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that Applications and ASG, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the IBAS master tape and thereby generate revenues for the Salem partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that Turi had met with the management and staff of ASG and Applications, and had become familiar with the contents and

operation of the IBAS program and the marketing potential of the IBAS master tape;

h. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and Global and Johnson, in the Global appraisal, represented that the fair market value, residual value,, and useful life attributed to the Salem equipment were reasonable and accurate;

i. The packagers and Lampf, in the Salem offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Salem appraisal, represented that the fair market value and useful life attributed to the IBAS master tape were reasonable and accurate.

359. These representations were false and misleading in that:

a. the IBM computer equipment described in the Salem offering memorandum did not exist or was not under lease to the end user, the Coleman Company, as represented;

b. the tax benefits and profits promised in the Salem offering memorandum and in the Lampf tax opinion could not be realized by the Salem plaintiffs;

c. the actual fair market value, residual value, and useful life of the Salem equipment were substantially less than represented;

d. the actual fair market value and useful life of the IBAS master tape were substantially less than represented;

e. the IBAS master tape was not readily marketable in its target market without substantial modifications in format;

f. on information and belief, the IBAS master tape program was not new or original, and therefore not qualified for investment tax credits;

g. ASG and Applications did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the IBAS master tape;

h. on information and belief, before issuing the TMS-Salem appraisal, Turi had not met with the management and staff of ASG and Applications, had not tested or run the IBAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the IBAS master tape.

360. In making the representations described above, the following Salem defendants failed to discuss the following material facts to the Salem plaintiffs:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Salem offering memorandum was not in fact the equipment owned by LCI or Analysis and purchased by the partnership;

b. The packagers, Lampf, Global, and Johnson failed to disclose that the IBM equipment described in the Salem offering memorandum was not currently under lease to the Coleman Company, the purported end user;

c. The packagers, Lampf, Global, and Johnson failed to disclose that the actual fair market value, residual value, and useful life of the Salem equipment were substantially less than represented in the Salem offering memoranda and in the Global appraisal;

d. The packagers, Lampf, Global, and Johnson failed to disclose that they had not performed any investigation to examine the Salem equipment or to verify its existence and condition;

e. The packagers, Lampf, Global, and Johnson failed to disclose that the Salem IBM equipment was essentially obsolete at the time it was purchased by the Salem partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, TMS, and Turi failed to disclose that the actual fair market value and useful life of IBAS master tape were substantially less than represented in the Salem offering memorandum and in the TMS-Salem appraisal;

g. The packagers, Lampf, TMS, and Turi failed to disclose that the IBAS master tape was not readily marketable in its target market without substantial modifications in format;

h. The packagers, Lampf, TMS, and Turi failed to disclose that the TMS-Salem appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

i. The packagers, Lampf, TMS, and Turi failed to disclose that before issuing the TMS-Salem appraisal, Turi had not met with the management and staff of ASG and Applications, had not tested or run the IBAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the IBAS master tape;

j. The packagers, Lampf, TMS, and Turi failed to disclose that, in order to achieve the market share projected in the TMS-Salem appraisal, the expenses of marketing the IBAS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

k. The packagers, Lampf, TMS, and Turi failed to disclose that ASG and Applications were undercapitalized and without sufficient skill, expertise, and personnel to market and license the IBAS master tape and generate revenues for the partnership; and

l. The packagers and Lampf failed to disclose that the Salem plaintiffs would not be entitled to the tax benefits

promised in the Salem offering memorandum and the Lampf tax opinion.

361. Defendants Johnson, Global, TMS, Turi, LCI, Analysis, Hernandez, Chandler, Anico, ASG, Applications, and Pine aided and abetted the misrepresentations and omissions alleged above in that their roles in the Salem partnership and their actions in furtherance of these roles, as described in paragraphs 354b-f above, were an essential component of the fraud perpetrated on the Salem plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on the Salem plaintiffs.

362. Beginning in and around December, 1980, and continuing until the present, the Salem defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around April, 1981, the packager defendants arranged for Mr. Turi to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Salem plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Salem equipment lease were current and that diligent efforts were being made to market and obtain licensees for the IBAS master tape, when in fact equipment lease payments owned to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

363. The Salem plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Salem defendants, as described herein. The Salem plaintiffs had no reason to believe that the Salem

defendants omitted to state material facts, as described herein. The Salem plaintiffs were not aware of the true facts or the facts that the Salem defendants omitted to state. The Salem plaintiffs were entitled to and did rely on the Salem defendants' representations, as described herein, and would not have purchased any interests in the Salem limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

364. The Salem plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

365. The Salem plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Salem plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 362 above. If the Salem plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 362 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

366. The Salem plaintiffs hereby tender their limited partnership interests to the Salem defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b))

373. The Salem plaintiffs reallege and incorporate by reference paragraphs 1-35, 353-366, above.

374. In connection with the sale of limited partnership interests in Salem Associates, defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf (the "Salem primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Salem plaintiffs; made untrue statements of material fact, as described in paragraphs 358-359 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 360 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Salem plaintiffs.

375. The Salem primary violators, and each of them, knew of the falsity of the representations described in paragraph 358 above, or recklessly failed to ascertain the truth of the representations. The Salem primary violators knew of the omissions of material fact described in paragraph 360 above, or recklessly failed to disclose these facts.

376. Defendants Analysis, Hernandez, Chandler, Anico, LCI, Global, Johnson, ASG, Applications, Pine, TMS, and Turi (the "Salem aiders and abettors") knew that their actions, as described in paragraphs 354b-f, 361 above, furthered and provided substantial assistance to the Salem primary violators in committing a fraud on the Salem plaintiffs.

377. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

378. As a result of these acts, the Salem plaintiffs are entitled to recover damages equal to all sums paid for

their investment, together with interest thereon since the date paid.

* * *

SIXTH CLAIM FOR RELIEF - TROY ASSOCIATES

The allegations in this Claim for Relief are made only on behalf of the Troy plaintiffs.

433. The Troy plaintiffs reallege and incorporate by reference paragraphs 1-35 above.

434. The following plaintiffs invested in the Troy Associates limited partnership in the amounts and on the dates indicated below. They shall be referred herein as the "Troy plaintiffs."

Plaintiff	Approximate Date of Investment	Approximate Total Amount Invested
John and Janice Gilbertson	6/81	$28,070.00
Donald H. Rundel	6/23/81	28,070.00
Cyril E. Harris	6/23/81	28,070.00
Thomas W. Hamilton	6/81	28,070.00
Thomas J. Hammond	6/81	14,035.00
Cameron & Wilson, a partnership	6/81	28,070.00
Charles F. Cameron	6/81	28,070.00
Peter C. Kirkman	6/81	28,070.00
Harold J. Peterson	6/81	28,070.00
George D. Morgan	6/81	14,035.00
Douglas E. Taylor	6/81	28,070.00
Donald J. DeFrancq	6/81	14,035.00
F. Paul Dickerson	6/81	56,140.00
Gary E. Grass	6/81	28,070.00
Richard G. Potter	6/25/81	28,070.00
Ernest DeFazio	6/29/81	28,070.00
Robert Scanlan	6/81	28,070.00

435. The following defendants participated in the Troy

Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Troy defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Troy partnership and were responsible for, among other things, the following:

(1) creating a Connecticut limited partnership, which was subsequently renamed Troy Associates;

(2) conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) soliciting and arranging for the installation of a general partner for the partnership;

(4) soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) soliciting and procuring other Troy defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) soliciting and procuring the services of defendant Arnheim & McCostis to act as general or special tax counsel for the partnership and to render a tax opinion for the partnership.

(7) instructing defendant Arnheim & McCostis with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, defendant LCA was also the immediate seller for the Troy partnership. As described in paragraph 6a above, in this capacity, it was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Troy equipment") purportedly consisted of an IBM 370/168 CPU,

an IBM 303 CPU, and approximately nineteen pieces of IBM peripheral equipment. The Troy partnership was to pay a total of $1,400,000 for this equipment. The master tape was of a software program known as Patient Accounting and Billing System ("PABS"), which was purportedly specially designed for routine accounting use by medical and dental offices and readily marketable within that industry. The Troy partnership was to pay a total of $2,400,000 for this master tape. Defendant LCA was comprised of defendants McKenna, Heitmeyer, and Wellbrock. LCA played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that, by purchasing the Troy equipment and the PABS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Troy partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCA was or should have been aware of its integral role in the Troy partnership and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself.

c. Defendant Rockwood was the equipment seller/lessee for the Troy partnership. As described in paragraph 6a above, in this capacity, it was the entity that sold the IBM equipment to the immediate seller, LCA, for resale to the Troy partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end users, which were represented to be C.I.T. Corporation and Spring Mills, Inc., and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Defendants Karnoff, Marks, and Costello were officers and controlling persons of Rockwood. Rockwood played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that, by selling the Troy equipment to LCA for resale to the Troy partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCA had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, also added credence to the reasonableness of the end user lease terms described in the Troy offering memorandum, and thus helped to substantiate the inf d price the partnership was to pay for the equipmen. As lessee of the equipment, Rockwood also provided the sale/leaseback scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Rockwood was or should have been aware of its integral role in the Troy partnership and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself.

d. Defendant Start Systems was the master tape lessee for the Troy partnership. As described in paragraph 6b above, in this capacity, it was the entity that leased the PABS master tape back from the Troy partnership and was to market and obtain licensees for the use of the master tape. Defendant Jeflen was an affiliate of Stuart Systems and was the master tape seller for the Troy partnership. As described in paragraph 6b above, in this capacity, it was the entity that sold the PABS master tape to LCA, the immediate seller, for resale to the Troy partnership. Defendants J. Feingold and L. Feingold were officers and controlling persons of Start Systems and Jeflen.

Jeflen, Start Systems, J. Feingold and/or L. Feingold had purportedly developed the PABS software program and had purported expertise in marketing the PABS master tape. On information and belief, J. Feingold and L. Feingold formed Jeflen and/or Start Systems solely for purposes of participating in the Troy partnership. Jeflen, J. Feingold, and L. Feingold played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that, by selling the PABS master tape to LCA for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCA had purchased the tape from an independent third party in an arm's length, negotiated transaction. Start Systems, J. Feingold, and L. Feingold played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that, by virtue of their purported expertise in the PABS software program and in the marketing of this software, they appeared capable of successfully exploiting the PABS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Jeflen, Start Systems, J. Feingold, and L. Feingold were or should have been aware of their integral role in the Troy partnership and of the lack of economic substance in these transactions in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves.

e. Defendant Computer Value was the equipment appraiser for the Troy partnership. Defendant Cuthbert was the president and controlling person of Computer Value. Defendants Computer Value and Cuthbert prepared a written appraisal of the Troy equipment, on or about February 25, 1981 (hereinafter "the Cuthbert-Troy appraisal") which appeared in the Troy offering memorandum, and which represented that the Troy equipment had a fair market value in excess of $1.45 million, that it had a useful life

of nine years, and that at the end of the nine years, it would have a residual value of at least $290,000. Computer Value and Cuthbert played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that the Cuthbert-Troy appraisal justified the inflated price the partnership was to pay for the Troy equipment and provided the limited partners with "independent" substantiation for the assumptions in the Troy offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user leases, from which the partnership would derive bonus rentals. Computer Value and Cuthbert were or should have been aware that the Cuthbert-Troy appraisal would be disseminated to prospective investors in Troy Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Cuthbert-Troy appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Troy equipment.

f. Defendant Information Industries was the master tape appraiser for the Troy partnership. Defendant Weber was an officer and controlling person of Information Industries. Defendants Information Industries and Weber prepared a written appraisal of the PABS master tape, on or about April 14, 1981, (hereinafter "the Weber appraisal") which appeared in the Troy offering memorandum, and which represented that the PABS master tape to be purchased from Jeflen and leased to Start Systems had a fair market value in excess of $2.6 million, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Troy partnership was paying for the PABS master tape was equal or close to this appraised fair market value. This appraisal also represented that defendant Weber had met

with the management of Jeflen and Start Systems, had examined in depth the design and structure of the PABS program, and had conducted an independent review of the potential market for the PABS master tape. Information Industries and Weber played an integral and essential role in the fraud perpetrated upon the Troy plaintiffs in that the Weber appraisal justified the inflated price the partnership was to pay for the PABS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Troy offering memorandum on which the promised tax benefits were based, i.e., that the purchase price of the PABS master tape was reasonable, that the tape was potentially profitable, and that it had a useful life of at least nine years. Information Industries and Weber were or should have been aware that the Weber appraisal would be disseminated to prospective investors in Troy Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Weber appraisal in making their investment decisions and to substantiate, for tax purposes, the fair market value and useful life of the PABS master tape.

g. Defendant Arnheim & McCostis was the general or special tax counsel for the Troy partnership. In this capacity, Arnheim & McCostis issued a special written tax opinion for the Troy partnership, in or about April, 1981, (hereinafter "the Arnheim & McCostis tax opinion") which appeared in the Troy offering memorandum, and upon which the Troy plaintiffs relied in making their investment in Troy Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax consequences to limited partners who had invested capital in Troy Associates. Arnheim & McCostis was paid at least $32,500 for preparing this tax opinion.

436. Beginning in or around April, 1981, and continuing to the present, the Troy defendants, in concert and conspiracy with one another, employed or aided and abetted

a device, scheme, or artifice to defraud the Troy plaintiffs in connection with the sale of limited partnership interests in Troy Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and leaseback the Troy computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Troy investors, in addition to income and profits.

437. The Troy plaintiffs were induced to invest in Troy Associates by means of an offering memorandum dated April 15, 1981, (hereinafter "the Troy offering memorandum"), which included the Arneheim & McCostis tax opinion, the Cuthbert-Troy appraisal, and the Weber appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 435b above, the end users that were purportedly already leasing this equipment, as described in paragraph 435c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 435b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 435e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Weber, was to be hired by the partnership to act as a consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

438. The Troy offering memorandum also stated that the packager defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the partic-

ipants in the Troy partnership had been, or would be, involved.

439. In connection with the sale of interests in Troy Associates to the Troy plaintiffs, the following defendants represented the following:

a. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, represented that the limited partnership investment would provide substantial tax benefits, as well as profit resulting from fees generated from licensing the PABS master tape and from the lease income and residual value in the Troy equipment;

b. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, represented that the Arnheim & McCostis tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Troy appraisal, represented that the Troy equipment existed, was specifically identified, and was already under lease to C.I.T. Corporation and Spring Mills, Inc. on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Information Industries and Weber, in the Weber appraisal, represented that the PABS master tape program was ready to market in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis

tax opinion, represented that the PABS master tape program was new and original, and therefore qualified for investment tax credits;

f. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Information Industries and Weber, in the Weber appraisal, represented that Start Systems and Jeflen, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the PABS master tape and thereby generate revenues for the Troy partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Information Industries and Weber, in the Weber appraisal, represented that Weber had met with the management of Jeflen and Start Systems, had become familiar with the design and structure of the PABS program, and had conducted independent research into the marketability of the PABS master tape;

h. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Troy appraisal, represented that the fair market value, residual value, and useful life attributed to the Troy equipment were reasonable and accurate;

i. The packagers and Arnheim & McCostis, in the Troy offering memorandum and the Arnheim & McCostis tax opinion, and Information Industries and Weber, in the Weber appraisal, represented that the fair market value and useful life attributed to the PABS master tape were reasonable and accurate.

440. These representations were false and misleading in that:

a. The IBM computer equipment described in the Troy offering memorandum did not exist or was not under lease to the end users, C.I.T. Corporation and Spring Mills, Inc., as represented;

b. The tax benefits and profits promised in the Troy offering memorandum and in the Arnheim & McCostis tax opinion could not be realized by the Troy plaintiffs;

c. The actual fair market value, residual value, and useful life of the Troy equipment were substantially less than represented;

d. The actual fair market value and useful life of the PABS master tape were substantially less than represented;

e. The PABS master tape was not readily marketable in its target market without substantial modifications in format;

f. On information and belief, the PABS master tape program was not new or original, and therefore not qualified for investment tax credits;

g. Start Systems and Jeflen did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the PABS master tape;

h. On information and belief, before issuing the Weber appraisal, Weber had not met with the management of Jeflen and Start Systems, had not tested or run the PABS program and was not familiar with its design and structure, and had not independently or adequately researched the marketability of the PABS master tape.

441. In making the representations described above, the following Troy defendants failed to disclose the following material facts to the Troy plaintiff;

a. The packagers and Arnheim & McCostis failed to disclose that the IBM equipment described in the Troy

offering memorandum was not in fact the equipment owned by LCA or Rockwood and purchased by the partnership;

b. The packagers, Arnheim & McCostis, Computer Value, and Cuthbert failed to disclose that the IBM equipment described in the Troy offering memorandum was not currently under lease to C.I.T. Corporation and Spring Mills, Inc., the purported end users;

c. The packagers, Arnheim & McCostis, Computer Value, and Cuthbert failed to disclose that the actual fair market value, residual value, and useful life of the Troy equipment were substantially less than represented in the Troy offering memorandum and in the Cuthbert-Troy appraisal;

d. The packagers, Arnheim & McCostis, Computer Value, and Cuthbert failed to disclose that they had not performed any investigation to examine the Troy equipment or to verify its existence and condition;

e. The packagers, Arnheim & McCostis, Computer Value, and Cuthbert failed to disclose that the Troy IBM equipment was essentially obsolete at the time it was purchased by the Troy partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Arnheim & McCostis, Information Industries, and Weber failed to disclose that the actual fair market value and useful life of the PABS master tape were substantially less than represented in the Troy offering memorandum and in the Weber appraisal;

g. The packagers, Arnheim & McCostis, Information Industries, and Weber failed to disclose that the Weber appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Arnheim & McCostis, Information Industries, and Weber failed to disclose that before issuing

the Weber appraisal, Weber had not met with the management of Jeflen and Start Systems, had not tested or run the PABS program and was not familiar with its design and structure, and had not independently or adequately researched the marketability of the PABS master tape;

i. The packagers, Lampf, Arnheim & McCostis, Information Industries, and Weber failed to disclose that the PABS master tape was not readily marketable in its target market without substantial modifications in format;

j. The packagers, Arnheim & McCostis, Information Industries, and Weber failed to disclose that, in order to achieve the market share projected in the Weber appraisal, the expenses of marketing the PABS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

k. The packagers, Arnheim & McCostis, Information Industries, and Weber failed to disclose that Start Systems and Jeflen were undercapitalized and without sufficient skill, expertise, and personnel to market and license the PABS master tape and generate revenues for the partnership; and

l. The packagers and Arnheim & McCostis failed to dislose that the Troy plaintiffs would not be entitled to the tax benefits promised in the Troy offering memorandum and the Arnheim & McCostis tax opinion.

442. Defendants Cuthbert, Computer Value, Weber, Information Industries, LCA, Rockwood, Karnoff, Marks, Costello, Start Systems, Jeflen, J. Feingold, and L. Feingold aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Troy partnership and their actions in furtherance of these roles, as described in paragraphs 435b-f above, were an essential

component of the fraud perpetrated on the Troy plaintiffs and provided substantial assistance to defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Arnheim & McCostis in committing a fraud on the Troy plaintiffs.

443. Beginning in and around April, 1981, and continuing until the present, the Troy defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and omissions described herein. In furtherance of this scheme and conspiracy, in or around September, 1981, the packager defendants arranged for Mr. Weber to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Troy plaintiffs, through periodic reports from The Lawrence Group, that lease payments on the Troy equipment lease were current and that diligent efforts were being made to market and obtain licensees for the PABS master tape, when in fact equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

444. The Troy plaintiffs had no reason to question or doubt the accuracy of any of the representations made by the Troy defendants, as described herein. The Troy plaintiffs had no reason to believe that the Troy defendants omitted to state material facts, as described herein. The Troy plaintiffs were not aware of the true facts or the facts that the Troy defendants omitted to state. The Troy plaintiffs were entitled to and did rely on the Troy defendants' representations, as described herein, and would not have purchased any interests in the Troy limited partnership had the misrepresentations of material facts not

been made or had the omissions of material facts not occurred.

445. The Troy plaintiffs did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March, 1986, after some plaintiffs conducted an investigation of the programs described herein following questioning by the IRS or certain tax deductions they had claimed based upon their investment in these partnerships.

446. The Troy plaintiffs were duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and defendant Lampf attempted to and did mislead the Troy plaintiffs and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 443 above. If the Troy plaintiffs or their agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and defendant Lampf, as described in paragraphs 8 and 443 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

447. The Troy plaintiffs hereby tender their limited partnership interests to the Troy defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10(b)

454. The Troy plaintiffs reallege and incorporate by reference paragraphs 1-35, 434-447, above.

455. In connection with the sale of the limited partnership interests in Troy Associates, defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Arnheim & McCostis (the "Troy primary violators"), and each of them, directly or by indirect means, and by the use of instru-

mentalities of interstate commerce and by the use of the mails, employed a device, scheme, and artifice to defraud the Troy plaintiffs; made untrue statements of material fact, as described in paragraphs 439-440 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 441 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon the Troy plaintiffs.

456. The Troy primary violators, and each of them, knew of the falsity of the representations described in paragraph 439 above, or recklessly failed to ascertain the truth of the representations. The Troy primary violators knew of the omissions of material fact described in paragraph 441 above, or recklessly failed to disclose these facts.

457. Defendants Rockwood, Karnoff, Marks, Costello, LCA, Start Systems, Jeflen, J. Feingold, L. Feingold, Computer Value, Cuthbert, Information Industries, and Weber (the "Troy aiders and abettors"), knew that their actions, as described in paragraphs 435b-f, 442 above, furthered and provided substantial assistance to the Troy primary violators in committing a fraud on the Troy plaintiffs.

458. The defendant primary violators' and aiders and abettors' acts as described herein constitute a violation of Section 10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j(b), and 17 C.F.R. 240.10b-5.

459. As a result of these acts, the Troy plaintiffs are entitled to recover damages equal to all sums paid for their investment, together with interest thereon since the date paid.

* * *

COMPLAINT IN *CATALAN* V. *PAULSON INVESTMENT CO., et al.*, Civ. No. 87-593-RE (D. ORE.)
(EXCERPTS)

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JURISDICTION AND VENUE

1. Count I arises under Section 17 (a) (1) of the Securities Act of 1933, 15 U.S.C. § 77q (a) (1). Jurisdiction for Count I is conferred by 15 U.S.C. § 77v. Count II arises under Section 10 of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j and 17 C.F.R. 240.10 (b)-5. Jurisdiction for count II is conferred by U.S.C. § 78aa. Count IV, V and VI arise under the Racketeer Influenced and Corrupt Organizations Act of 1970 ("RICO"), 18 U.S.C. §§ 1964. Jurisdiction for these Counts is conferred by 18 U.S.C. §§ 1964 and 1965. Jurisdiction for count III and Counts VII through XIV arise under the principles of pendent jurisdiction.

2. Venue is proper in this district in that the acts alleged herein took place in whole or in part in Oregon, including the sales of the securities described herein, and the Plaintiff's claim arose in this district.

DESCRIPTION OF THE PROGRAMS

3. This action arises out of the packaging, syndication, promotion and sale in Oregon of a tax shelter limited partnership interest to Plaintiff Anthony Catalan, As more particularly described herein, the tax shelter involved the purchase and lease back of certain IBM computer hardware equipment and certain so-called master tapes of computer software programs. The Plaintiff invested in the tax shelter by purchasing a limited partnership unit in a limited partnership known as Columbia Associates.

4. The Columbia Associates limited partnership was promoted and sold during the 1979, 1980 or 1981, to general partners and then to investors as "pre-packaged" programs. The Plaintiff purchased his limited partnership in-

terest through Lynn Hammersly of Defendant Paulson Investment Co., Inc. The Columbia Associates limited partnership had the following characteristics:

a. The partnership was packaged and promoted by the same group of six Defendants ("the packagers"), as described more particularly herein.

b. The partnership was comprised of 35 limited partnership "units" and was designed to raise approximately one million dollars.

c. The partnership was to enter into identically structured sale and lease back transactions with respect to the computer equipment and master tape, as described more particularly herein.

d. The partnership was created as a Connecticut limited partnership.

e. The offering memoranda used to promote and sell the partnerships were virtually identical in format and in content as other limited partnerships promoted and sold by Defendants in Oregon and elsewhere during this same time period.

f. The tax opinion, equipment appraisal and master tape appraisal contained in the offering memorandum was virtually identical in format and content as used in other offering memoranda of other limited partnerships promoted and sold by Defendants in Oregon and elsewhere during this same time period.

5. The Columbia Associates limited partnership was similar to at least twelve other tax shelter limited partnerships packaged and promoted by the packager Defendants in Oregon and elsewhere during this same time period, including the limited partnerships known as Troy Associates, Runnels Associates, Lake Associates, Mars Associates, Victoria Associates, Travis Associates, K-T Associates, Bandera Associates, Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum Associates.

6. The tax benefits purportedly to be derived from investing in the Columbia Associates limited partnership described herein was to be achieved through a complex series of purchase, sale and lease back transactions, structured and arranged by the packager Defendants. As described in the offering memoranda used to promote and sell the investments, these transactions were to be structured as follows:

a. The Equipment Transactions

(1) The partnership was to purchase certain specified IBM computer hardware equipment (the "equipment") from an identified entity. This entity was the immediate seller of the equipment to the partnership and will hereinafter be referred to as the "immediate seller." The partnership was to pay less then ten percent of the purchase price of the equipment in case at closing, and the remainder was to be financed by a nine-year non-recourse note. The equipment was purportedly already subject to a bank debt at the time of this transaction.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the equipment from another identified entity (the "equipment seller") for resale to the partnership.

(3) Simultaneously with purchasing the equipment from the immediate seller, the partnership was to lease the equipment back to the equipment seller under a non-cancellable nine-year lease. The equipment seller would thereby become a lessee of the equipment from the partnership. This entity will hereinafter be referred to as the "equipment seller/lessee."

(4) At the time of all these transactions, the equipment was represented to be already in place and in use by one or more identified nationally recognized companies (the "user"). The user had purportedly leased the equipment from the equipment seller/lessee before it was sold

to the immediate seller for resale to the partnership. This underlying lease (the "user lease") was to expire within 36 to 48 months, at which time the equipment was to be re-leased to another user, if possible. During the pendency of any such subsequent user lease, the partnership was to receive a specified "bonus rental" of approximately 50 percent of the subsequent user's lease payments.

b. The Master Tape Transactions

(1) In addition to and simultaneously with purchasing the computer equipment, the partnership was to also purchase a master tape for certain specific computer software (the "master tape") from the same immediate seller from whom it had purchased the computer equipment. The master tape was purportedly designed for a specialized function or for use in a specific identified industry, and was purportedly readily marketable for that function or within that industry. The partnership was to pay less than ten percent of the purchase price of the master tape in cash at closing, and the remainder was to be financed by a long-term note of approximately 20 years. In addition, each partner in the partnership was to execute a "personal liability agreement" making him or her personally liable for his or her pro-rata share of the partnership's liability on the master tape note.

(2) Just prior to this sale to the partnership, the immediate seller had purportedly purchased the master tape from another identified entity (the "master tape seller") for resale to the partnership.

(3) Simultaneously with purchasing the master tape from the immediate seller, the partnership was to lease the master tape back to an identified affiliate of the master tape seller. This entity will hereinafter be referred to as the "master tape lessee."

(4) The master tape lessee was to market and license the master tape to businesses or entities that were in need

of the specialized function the software could perform or within the specific industry for which the software was designed. Revenues generated from marketing and licensing the master tape were to be shared with the partnership in the form of certain specified flat and percentage fees paid to the partnership.

7. The offering memorandum issued to promote and sell the Columbia Associates limited partnership and to attract potential investors contained, among other things, the following:

a. A description of the transactions as outlined above;

b. A purportedly independent appraisal of the computer equipment, including an appraisal and valuation of its fair market value, residual value and useful life;

c. A purportedly independent appraisal of the master tape, including an appraisal and valuation of its fair market value and useful life, and a description of potential markets and licensees for the master tape; and

d. A tax opinion letter by Defendant Lampf describing the tax benefits to be derived form investing in the partnership, including eligibility for an investment tax credit for the master tape transaction, depreciation of both equipment and master tape, and for investor interest expense, and partnership trade or business expenses and losses.

8. In or around April and/or October 1984, in connection with the settlement of litigation against them relating to the limited partnerships known as Evergreen Associates, Celica Associates, Maverick Associates, and Yoakum Associates, the packager Defendants and Defendant Lampf arranged to have all documents and materials relating to or generated in that litigation kept confidential and/or sealed by the Court.

DESCRIPTION OF THE PLAINTIFF

9. The Plaintiff invested in the Columbia Associates limited partnership in the amount of $26,805.00 between December 17, 1980, and January 28, 1982.

DESCRIPTION OF THE DEFENDANTS

The Packagers

10. Defendants Leasing Consultants Associates ("LCA"), Leasing Consultants, Inc. ("LCI"), William L. McKenna ("McKenna"), Richard A. Heitmeyer ("Heitmeyer"), Richard D. Wellbrock ("Wellbrock") and William B. Ward ("Ward") acted as packagers and promoters of the tax shelter program sold to Plaintiff, and conceived and arranged for the sale, purchase and lease transactions involved, procured the services of Lampf and other Defendants, caused the preparation and dissemination of a model offering memorandum, solicited and procured broker/dealers and others to place or sell the limited partnership interest to Plaintiff, and solicited and procured appraisals for the equipment and master tapes.

11. Defendant LCA was at all relevant times a New Jersey general partnership comprised of Defendants McKenna, Heitmeyer and Wellbrock.

12. Defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey, and was an affiliate of Defendant LCA. Defendants McKenna, Heitmeyer, Wellbrock and Ward were officers and controlling persons of LCI and were, at all relevant times, citizens of the State of New Jersey.

The Immediate Sellers

13. As described above, Defendant LCA was at all relevant times a New Jersey general partnership.

14. As described above, Defendant LCI was at all relevant times a Delaware corporation with its principal place of business in New Jersey.

15. Defendant American Computer Equipment Leasing, Inc. ("ACE") was at all relevant times a corporation doing business in the State of New York.

16. Defendant Computer Systems Consultants, Inc. ("CSC") was at all relevant times a Delaware corporation with its principal office in Ridgewood, New Jersey.

The Equipment Sellers/Lessees

17. Defendant Analysis International Co., Inc. ("Analysis") is or was a corporation with its principal place of business in Charlotte, North Carolina. Defendant Anico Computer Leasing, Inc. ("Anico") is or was a North Carolina corporation and the parent corporation and controlling person of Defendant Analysis. Defendants Amato Hernandez ("Hernandez") and John Chandler ("Char dler") are or were officers and controlling persons of Analysis and Anico.

18. Defendant Alanthus Computer Corporation ("Alanthus Computer") and Defendant Alanthus Corporation ("Alanthus") are or were Delaware corporations. On information and belief, Alanthus Computer and/or Alanthus are now known as Technology Finance Group. On information and belief, Alanthus Computer and /or Alanthus may have been affiliated with Analysis International Co., Inc.

a. Defendant Comdisco, Inc. ("Comdisco") is or was a corporation doing business in the State of Illinois, and Defendant Kenneth Pontikes ("Pontikes") is or was an officer and controlling person of Comdisco.

The Master Tape Lessees and Affiliates

19. Defendants Kirby Microprocessors, Inc. ("KMI") and Kirby Computer Systems, Inc. ("Kirby Computer") were

at all relevant times corporations doing business in the State of New Jersey. Defendant Robert M. Kirby ("Kirby") is or was the owner and controlling person of KMI and Kirby Computer.

20. Defendants Gordon S. Rosen Associates, Inc. ("Rosen Associates") and Software Systems for Word Processors, Inc. ("SSWPI") were at all relevant times corporations doing business in the State of New York. Defendant Gordon S. Rosen ("Rosen") is or was the owner and controlling person of Rosen Associates and SSWPI.

21. Defendants Robrech Systems, Inc. ("Robrech") and Digitize, Inc. ("Digitize") were at all relevant times corporations doing business in the State of New York.

22. Defendants Buhler Software Services ("Buhler Software") and P-STAT, Inc. ("P-Stat") were at all relevant times corporations doing business in the State of New Jersey. Defendant Roald Buhler ("Buhler") is or was the owner and controlling person of Buhler Software and P-Stat.

23. Defendants ASG Program Products, Inc. ("ASG") and Applications Systems Group, Inc. ("Applications") were at all relevant times corporations doing business in the State of New York. Defendant Martin D. Pine ("Pine") is or was the president and/or controlling person of ASG and Application.

a. Defendant Mark Hanson was at all relevant times the president and controlling person of two entities known as Prose, Inc. and M. A. Hanson & Associates which were a corporation entity doing business in the State of Pennsylvania.

The Equipment Appraisers

24. Defendant Computer Value Associates ("Computer Value") was at all relevant times a company doing business

in the State of New York. Defendant James Cuthbert ("Cuthbert") is or was the president and controlling person of Computer Value.

25. Defendants Texcom Equipment Corporation ("Texcom") and Global Computer Corporation ("Global") were at all relevant times corporations doing business in the State of Texas. Defendant Ronald Johnson ("Johnson") is or was the president, owner, and controlling person of Texcom and Global.

26. Defendant Berlent Industries, Inc. ("Berlent Industries") was at all relevant times a corporation doing business in the State of New York. Defendant Harvey N. Berlent ("Berlent") is or was the president and controlling person of Berlent Industries.

The Master Tape Appraisers

27. Defendant Ward was at all relevant times a citizen of the State of New Jersey.

28. Defendant ConServ International, Inc. ("ConServ") was at all relevant times a corporation doing business in the State of New. Jersey. Defendant Robert W. Steinberger ("Steinberger") is or was the president and controlling person of ConServ. Prior to his association with ConServ, Steinberger was vice president of Defendant Kirby Computer.

29. Defendant Technical Marketing Services, Inc. ("TMS") was at all relevant times a corporation doing business in the States of New York and New Jersey. Defendant Leonard F. Turi ("Turi") is or was the president and controlling person of TMS.

a. Defendant Edward Fizell was at all relevant times a citizen of the State of New Jersey.

The Attorneys

30. Defendant Lampf, Pleva, Lipkind, Prupis & Petigrow, P.C. ("Lampf") was at all relevant times a professional legal corporation with its principal place of business in the State of New Jersey. Lampf is now known as Lampf, Lipkind, Prupis & Petigrow, P.C.

The General Partnership

31. The packagers solicited and arranged for James D. Quenemoen and Robert G. Williams of Columbia Associates, Portland, Oregon, to act as general partners for their partnership and were responsible for, among other things, the following:

a. Soliciting and procuring various broker/dealers and individuals to purchase interest in the limited partnership;

b. Utilizing services of the Defendant attorneys to acts as tax counsel for the Columbia Associates limited partnership;

c. Preparing and distributing a memorandum to Defendant broker Paulson Investment Co., Inc., modeled after the memorandum offered to Columbia Associates by the Defendant packagers.

32. Defendant Columbia Associates was at all relevant times an Oregon general partnership comprised of James D. Quenemoen and Robert G. Williams, who are citizens of the State of Oregon.

The Brokerage Firm

33. The packagers and/or Columbia Associates solicited and procured broker/dealers to place or file interest in the limited partnerships. Paulson Investment Co., Inc., was such a broker/dealer who was responsible for, among other things, soliciting and procuring Plaintiff Catalan into purchasing an interest in the limited partnership; utilizing and distributing a memorandum, prepared by Columbia Associates and modeled after the memorandum offered by the Defendant packagers.

34. Defendant Paulson Investment Co., Inc., was at all relevant times an Oregon corporation with its principal place of business in Oregon. Chester Paulson was the president and controlling person of Paulson Investment Co., and was at all relevant time, a citizen of the State of Oregon.

Non-Defendant Co-Conspirators

35. The Lawrence Group was at all material times a consulting firm controlled by Defendant William Ward. After the sales of the limited partnership unites described herein, the Lawrence Group was engaged by the partnerships, at the suggestion of the packager Defendants, purportedly to monitor the status of each of the partnerships' equipment and master tape leases and to make periodic reports to the partnerships describing this status.

ALLEGATIONS COMMON TO ALL CLAIMS FOR RELIEF

36. Plaintiff realleges and incorporates by reference paragraphs 1 through 35 above.

37. The following Defendants participated in the Columbia Associates limited partnership in the following capacities. They shall sometimes hereinafter be collectively referred to as the "Columbia Defendants."

a. Defendants LCA, LCI, McKenna, Heitmeyer, Wellbrock, and Ward packaged and promoted the Columbia partnership and were responsible for, among other things, the following:

(1) Creating a Connecticut limited partnership, which was subsequently renamed Columbia Associates;

(2) Conceiving, arranging for and structuring the purchase, sale and lease transactions for the partnership;

(3) Soliciting and arranging for the installation of a general partner for the partnership;

(4) Soliciting and procuring broker/dealers and others to place or sell interests in the partnership;

(5) Soliciting and procuring other Columbia Defendants to act as sellers, lessees, and appraisers of the partnership's equipment and master tape;

(6) Soliciting and procuring the services of Defendant Lampf to: act as special tax counsel for the partnership, render a tax opinion for the partnership, prepare, print, and distribute a model offering memorandum on which the Columbia offering memorandum was based and prepare, print, and distribute a model partnership agreement and model sales and lease agreements on which the columbia partnership agreement and sales and lease agreements were based; and

(7) Instructing Defendant Lampf with respect to disbursements of subscription proceeds from the escrow account maintained on behalf of the partnership.

b. In addition to its role as a packager, Defendant LCI was also the immediate seller for the Columbia partnership. As described in paragraph 6a above, in this capacity, LCI was the entity that purchased the IBM equipment and the master tape from the equipment seller and the master tape seller, and then resold the equipment and master tape to the partnership. This equipment (hereinafter the "Columbia equipment") purportedly consisted of two IBM 370/158 CPU's, an IBM 3800 Printing Subsystem, and approximately thirteen pieces of IBM peripheral equipment. The Columbia partnership was to pay a total of 1.45 million dollars for this equipment. The master tape was of a software program known as Office Automation System ("OAS"), which was purportedly specially designed to perform basic accounting functions, such as payroll and receivables, on Xerox and Wang Word processing units, and was purportedly readily marketable to businesses having those makes of word processing units. The Columbia partnership was to pay a total of 1.95 million

dollars for this master tape. Defendants McKenna, Heitmeyer, Wellbrock, and Ward were principals and controlling persons of Defendant LCI. LCI played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, by purchasing the Columbia equipment and the OAS master tape from the equipment seller and the master tape seller, and then reselling this equipment and master tape to the Columbia partnership, it obscured the original purchase price of the equipment and master tape, provided a means by which the price of the equipment and master tape could be inflated, and gave the partnership's purchase of the equipment and master tape the appearance of an arm's length transaction at a negotiated, fair market price. LCI was or should have been aware of its integral role in the Columbia offering and of the lack of economic substance in these transactions in that it both bought and sold the equipment and master tape on the same day at a substantial profit with virtually no risk to itself, and with knowledge or reason to know that the equipment and master tape would be used by the packagers in a limited partnership offering. LCI knew or should have known its equipment and master tape transactions described herein would be used to induce these investors to invest in the partnership, and that these investors would rely upon the terms of these transactions in making their investment decisions and to substantiate, for tax purposes, the fair market value, useful life, title and residual value of the equipment, and the fair market value and useful life of the master tape.

c. Defendant Analysis was the equipment seller/lessee for the Columbia partnership. As described in paragraph 6a above, in this capacity, Analysis was the entity that sold the Columbia equipment to the immediate seller, LCI, for resale to the Columbia partnership, and then leased the equipment back from the partnership. It was also the entity that had, purportedly, previously leased the equipment to the end users, which were represented to be W. R.

Grace & Company, Westinghouse Electric Corporation, and Spring Mills, Inc., and was to re-lease the equipment to one or more subsequent end users when the existing user leases expired. Defendant Anico was the parent corporation and a controlling person of Analysis. Defendants Hernandez and Chandler were officers and controlling persons of Analysis. Analysis played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, by selling the Columbia equipment to LCI for resale to the Columbia partnership, it further obscured the original purchase price of the equipment, provided part of the justification for the inflated price the partnership was to pay for the equipment, and provided the illusion that LCI had purchased the equipment from an independent third party at an arm's length, negotiated price. By acting as lessee of the equipment, Analysis also added credence to the reasonableness of the end user lease terms described in the columbia offering memorandum, and thus helped to substantiate the inflated price the partnership was to pay for the equipment. As lessee of the equipment, Analysis also provided the sale/lease back scheme with an entity that would relieve the partnership of any responsibility to re-lease the equipment at the expiration of the end user leases, in anticipation of a probable IRS objection to the economic substance of these transactions if the partnership had to seek its own lessees. Analysis was or should have been aware of its integral role in the Columbia offering and of the lack of economic substance in these transactions in that it made a substantial profit as a result of these transactions with little or no risk to itself, and with knowledge or reason to know that the equipment would be used by the packagers in a limited partnership offering. Analysis knew or should have known the equipment transactions described herein would be used to induce investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes,

the fair market value, title, useful life and residual value of the equipment.

d. Defendant SSWPI was the master tape lessee for the Columbia partnership. As described in paragraph 6b above, in this capacity, SSWPI was the entity that leased the OAS master tape back from the Columbia partnership and was to market and obtain licensees for the use of the master tape. Defendant SSWPI was an affiliate of Rosen Associates, which was the master tape seller for the Columbia partnership. As described in paragraph 6b above, in this capacity, Rosen Associates was the entity that sold the OAS master tape to LCI, the immediate seller, for resale to the Columbia partnership. Defendant Rosen was the owner and controlling person of Rosen Associates and SSWPI. Rosen Associates, SSWPI, and/or Rosen had purportedly developed the OAS software program and had purported expertise in marketing the OAS master tape. On information and belief, Rosen formed Rosen Associates and/or SSWPI solely for purposes of participating in the Columbia partnership. Rosen Associates and Rosen played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, by selling the OAS master tape to LCI for resale to the partnership, they made the purchase price of the tape appear reasonable by making it appear as if LCI had purchased the tape from an independent third party in an arm's length, negotiated transaction. SSWPI and Rosen played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, by virtue of their purported expertise in the OAS software program and in the marketing of this software, they appeared capable of successfully exploiting the OAS master tape, and thus gave credence to the ambitious market-share goals and profit projections used by the master tape appraiser to justify the inflated valuation of the tape. Rosen Associate, SSWPI, and Rosen were or should have been aware of their integral role in the Columbia offering and of the lack of economic substance in these transactions

in that they made or stood to make a substantial profit as a result of these transactions with little or no capital outlay and little or no risk to themselves, and with knowledge or reason to know that the OAS master tape would be used by the packagers in a limited partnership offering. Rosen Associates, SSWPI, and Rosen knew or should have known that the OAS master tape transactions described herein would be used to induce the investors to invest in the partnership, and that the investors would rely on the terms of the transactions in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the OAS master tape.

e. Defendant Computer Value was the equipment appraiser for the Columbia partnership. Defendant Cuthbert was the president and controlling person of Computer Value. Defendants Computer Value and Cuthbert prepared a written appraisal of the Columbia equipment, on or about September 29, 1980 (hereinafter "the Cuthbert-Columbia appraisal"), which appeared in the Columbia offering memorandum, and which represented that the Columbia equipment had a fair market value of 1.5 million dollars, a useful life in excess of nine years, and a residual value at the end of nine years in excess of $300,000.00. Computer Value and Cuthbert played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, the Cuthbert-Columbia appraisal justified the inflated price the partnership was to pay for the Columbia equipment and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the equipment was reasonable, that it had a useful life of at least nine years, and that it would have a substantial residual value, after the expiration of the end user leases, from which the partnership would derive bonus rentals. Computer Value and Cuthbert were or should have been aware that the Cuthbert-Columbia appraisal would be disseminated to pro-

spective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the Cuthbert-Columbia appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value, residual value, and useful life of the Columbia equipment.

f. Defendant TMS was the master tape appraiser for the Columbia partnership. Defendant Turi was the president and controlling person of TMS. Defendants TMS and Turi prepared a written appraisal of the OAS master tape, on or about October 31, 1980 (hereinafter "the TMS-Columbia appraisal"), which appeared in the Columbia offering memorandum, and which represented that the fair market value of the OAS master tape to be purchased from Rosen Associates and leased to SSWPI was in excess of 3.4 million dollars, and that it had a useful life of at least nine years. This appraisal also represented that the purchase price that the Columbia partnership was paying for the OAS master tape was equal or close to this appraised fair market value. This appraisal also represented that Defendant Turi had met with the management and technical staff of Rosen Associates and SSWPI, had examined in detail the contents of the OAS master tape, and had discussed with Rosen Associates and SSWPI the underlying objectives of the OAS program, its current development and operational status, the marketing plans contemplated by SSWPI, and the market segments that could benefit from licensing the OAS master tape. TMS and Turi played an integral and essential role in the fraud perpetrated upon the Plaintiff in that, the TMS-Columbia appraisal justified the inflated price the partnership was to pay for the OAS master tape and provided the limited partners with "independent" substantiation for the assumptions in the Columbia offering memorandum on which the promised tax benefits were based, *i.e.*, that the purchase price of the OAS master tape was reasonable, that the tape was potentially profitable, and that it had a useful

life of at least nine years. TMS and Turi were or should have been aware that the TMS-Columbia appraisal would be disseminated to prospective investors in Columbia Associates and would be used to induce these investors to invest in the partnership, and that these investors would rely upon the TMS-Columbia appraisal in making their investment decisions, and to substantiate, for tax purposes, the fair market value and useful life of the OAS master tape.

g. Defendant Lampf was the special tax counsel for the Columbia partnership. In this capacity, Lampf issued a special written tax opinion for the Columbia partnership, on or about October 1980 (hereinafter "the Lampf tax opinion"), which it knew would appear in the Columbia offering memorandum, and upon which it knew potential investors, including the Plaintiff, would rely in making their investment in Columbia Associates. As stated in the tax opinion, the purpose of the opinion was to set forth certain federal income tax benefits to limited partners who had invested capital in Columbia Associates, as more particularly alleged in paragraph 7d. Lampf was paid at least $20,000.00 for preparing this tax opinion. Lampf also prepared, printed, and distributed a model offering memorandum, on which the Columbia offering memorandum was based. Lampf also prepared, printed, and distributed a model partnership agreement and model sale and lease agreements, on which the columbia partnership agreement and sale and lease agreements were based.

38. Beginning in or around November 1980, and continuing to the present, the Columbia Defendants, in concert and conspiracy with one another, employed or aided and abetted a device, scheme, or artifice to defraud the Plaintiff in connection with the sale of limited partnership interests in Columbia Associates, as described more particularly below. These limited partnership interests constitute investment contracts and securities, and consisted of a tax shelter program to purchase and lease back the

Columbia computer equipment and master tape described above. This program was purportedly designed to generate substantial tax benefits to the Columbia investors, as more particularly alleged in paragraph 7d, in addition to income and profits.

39. The Plaintiff was induced to invest in Columbia Associates by means of an offering memorandum dated November 14, 1980, and a supplemental offering memorandum dated December 29, 1980 (hereinafter collectively "the Columbia offering memorandum"), which included the Lampf tax opinion, the Cuthbert-Columbia appraisal, and the TMS-Columbia appraisal. This offering memorandum described, among other things, the IBM computer equipment to be purchased and leased back by the partnership, as described in paragraph 37b above, the end users that were purportedly already leasing this equipment, as described in paragraph 37c above, the master tape to be purchased and leased back by the partnership, as described in paragraph 37b above, the fair market value, residual value, and useful life of the equipment and master tape, as described in paragraphs 37e-f above, and the tax benefits and profits to be derived from investing in the partnership, as described in paragraph 7d above. This offering memorandum also represented that the partnership's master tape appraiser, Mr. Turi, was to be hired by the partnership to act as consultant to the partnership to periodically review the partnership's activities and monitor the revenues received by the partnership.

40. The Columbia offering memorandum also stated that the packager Defendants had had transactions in the past, and contemplated transactions in the future, in which they sold or brokered computer equipment and/or master tapes to other partnerships in which some or all of the participants in the Columbia partnership had been, or would be, involved. This offering memorandum also stated that Defendant Lampf had acted in the past, and anticipated acting in the future, as counsel to other partnerships in

which some or all of the participants in the Columbia partnership had been, or would be involved.

41. In connection with the sale of interest in Columbia Associates to the Plaintiff, the following Defendants represented the following:

a. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the limited partnership investment would provide substantial profits resulting from fees generated form licensing the OAS master tape and from the lease income and residual value in the Columbia equipment;

b. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the lampf tax opinion supported the investors' entitlement to tax benefits and the legitimacy of the program under existing applicable laws;

c. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the Columbia equipment existed, was specifically identified, and was already under lease to W. R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., on terms that would provide sufficient income to cover the lease payments to the seller;

d. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the OAS master tape program was ready to be marketed in its then-existing format and would readily achieve a substantial market share in its target market;

e. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, represented that the OAS master tape program was tangible, new and original and previously unexploited property, and therefore qualified for investment tax credits;

f. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that SSWPI and Rosen Associates, the master tape lessee and its affiliate, despite their small size, were skilled enough and possessed the required capital, expertise, ability, and personnel to successfully market and obtain licensees for the OAS master tape and thereby generate revenues for the Columbia partnership sufficient to repay the seller for its purchase price and to make a profit for the partnership;

g. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the management and staff of Rosen Associates and SSWPI, and had become familiar with the contents and operation of the OAS program and the marketing potential of the OAS master tape;

h. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and Computer Value and Cuthbert, in the Cuthbert-Columbia appraisal, represented that the fair market value, residual value, and useful life attributed to the Columbia equipment were reasonable and accurate;

i. The packagers and Lampf, in the Columbia offering memorandum and the Lampf tax opinion, and TMS and Turi, in the TMS-Columbia appraisal, represented that the fair market value and useful life attributed to the OAS master tape were reasonable and accurate.

42. These representations were false and misleading in that:

a. The IBM computer equipment described in the Columbia offering memorandum did not exist or was not under lease to the end users, W. R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., as represented;

b. The profits promised in the Columbia offering memorandum and in the Lampf tax opinion could not be realized by the Plaintiff;

c. The actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented;

d. The actual fair market value and useful life of the OAS master tape were substantially less than represented;

e. The OAS master tape was not readily marketable in its target market without substantial modifications in format;

f. On information and belief, the OAS master tape program was not tangible, new, original or previously unexploited property, and therefore not qualified for investment tax credit;

g. Rosen Associates and SSWPI did not possess the skill, ability, personnel, or financial wherewithal to successfully market or license the OAS master tape;

h. On information and belief, before issuing the TMS-Columbia appraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation and had not adequately investigated the marketability of the OAS master tape.

43. In making the representations described above, the following Columbia Defendants failed to disclose the following material facts to Plaintiff:

a. The packagers and Lampf failed to disclose that the IBM equipment described in the Columbia offering memorandum was not in fact the equipment owned by LCI or Analysis and purchased by the partnership;

b. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the IBM equipment described

in the columbia offering memorandum was not currently under lease to W. R. Grace & Co., Westinghouse Electric, and Spring Mills, Inc., the purported end users;

c. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the actual fair market value, residual value, and useful life of the Columbia equipment were substantially less than represented in the columbia offering memorandum and in the Cuthbert-Columbia appraisal;

d. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that they had not performed any investigation to examine the Columbia equipment or to verify its existence and condition;

e. The packagers, Lampf, Computer Value, and Cuthbert failed to disclose that the Columbia IBM equipment was essentially obsolete at the time it was purchased by the columbia partnership in that IBM had already announced the introduction of new, better systems that would render the equipment obsolete;

f. The packagers, Lampf, TMS, and Turi failed to disclose that the actual market value and useful life of the OAS master tape were substantially less than represented in the Columbia offering memorandum and in the TMS-Columbia appraisal;

g. The packagers, Lampf, TMS, and Turi failed to disclose that the TMS-Columbia appraisal contained income projections for valuation purposes that were made without a reasonable basis in fact;

h. The packagers, Lampf, TMS, and Turi failed to disclose that before issuing the TMS-Columbia appraisal, Turi had not met with the management and staff of Rosen Associates and SSWPI, had not tested or run the OAS program and was not familiar with its contents and operation, and had not adequately investigated the marketability of the OAS master tape;

i. The packagers, Lampf, TMS and Turi failed to disclose that, in order to achieve the market share projected in the TMS-Columbia appraisal, the expenses of marketing the OAS master tape would be enormous, and that these expenses would need to be paid out of any gross revenues received from licensing the master tape before any profit could be returned to the partnership;

j. The packagers, Lampf, TMS, and Turi failed to disclose that Rosen Associates and SSWPI were undercapitalized and without sufficient skill, expertise, and personnel to market and license the OAS master tape and generate revenues for the partnership;

k. The packagers, Lampf, TMS, and Turi failed to disclose that the OAS master tape was not readily marketable in its target market without substantial modifications in format; and

l. The packagers, Lampf, Analysis, Computer Value, and Cuthbert failed to disclose that the Columbia partnership would not and could not obtain title to the Columbia equipment because of the terms and nature of preexisting transactions involving the Columbia equipment.

44. Defendants Cuthbert, Computer Value, TMS, Turi, LCI, Analysis, Hernandez, Chandler, Anico, Rosen Associates, SSWPI, and Rosen aided and abetted in the misrepresentations and omissions alleged above in that their roles in the Columbia partnership and their actions in furtherance of these roles, as described in paragraphs 37b-f above, were essential components of the fraud perpetrated on Plaintiff and provided substantial assistance to Defendants LCI, LCA, McKenna, Heitmeyer, Wellbrock, Ward, and Lampf in committing a fraud on Plaintiff.

45. Beginning in and around November 1980, and continuing until the present, the Columbia Defendants, and each of them, combined and conspired with each other in an effort to commit and conceal the wrongful acts and

omissions described herein. In furtherance of this scheme and conspiracy, in or around April, 1981, the packager Defendants arranged for Mr. Turi to be replaced by The Lawrence Group to act as consultant to the partnership and continually assured and represented to the Plaintiff, through periodic reports from The Lawrence Group, that lease payments on the Columbia equipment lease were current and that diligent efforts were being made to market and obtain licensees for the OAS master tape when, in fact, equipment lease payments owed to the partnership were sometimes delinquent, and little or no effort was being made to market and obtain licensees for the master tape. To the extent that any problems were identified in these Lawrence Group reports concerning the equipment lease or the master tape marketing, they were attributed to unanticipated events or market trends.

46. Plaintiff had no reason to question or doubt the accuracy of any of the representations made by the Columbia Defendants, as described herein. Plaintiff had no reason to believe that the Columbia Defendents omitted to state material facts, as described herein. Plaintiff was not aware of the true facts or the facts that the Columbia Defendants omitted to state. Plaintiff was entitled to and did rely on the Columbia Defendants' representations, as described herein, and would not have purchased any interests in the Columbia limited partnership had the misrepresentations of material facts not been made or had the omissions of material fact not occurred.

47. The Plaintiff did not discover and could not reasonably have discovered the facts giving rise to the claims asserted herein until at least March 1986, after he conducted an investigation of the programs described herein following questioning by the IRS of certain tax deductions they had claimed based upon their investment in these partnerships.

48. Plaintiff was duly diligent in attempting to uncover the facts giving rise to the claims asserted herein. The packagers and Lampf attempted to and did mislead the Plaintiff and conceal the fraud alleged herein by means of the affirmative acts described in paragraphs 8 and 45 above. If Plaintiff or his agents knew of any facts potentially constituting the claims asserted herein, then the conduct of the packagers and Lampf, as described in paragraphs 8 and 45 above, led them, under the circumstances described herein, to disregard those facts and to reasonably believe that they did not have a claim for relief.

49. Plaintiff hereby tenders his limited partnership interest to the Columbia Defendants.

* * *

COUNT II

(1934 Securities Exchange Act - Section 10 (b))

56. Plaintiff realleges and incorporates by reference paragraphs 1 through 49 above.

57. In connection with the sale of the limited partnership interests in Columbia Associates, Defendants LCI, LCA, McKenna, Wellbrock, Ward, and Lampf (the "Columbia primary violators"), and each of them, directly or by indirect means, and by the use of instrumentalities of interstate commerce and by use of the mails, employed a device, scheme, and artifice to defraud the Plaintiff; made untrue statements of material fact, as described in paragraphs 41-42 above, and omitted to state material facts necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, as described in paragraph 43 above; and engaged in acts, practices, and a course of business designed to operate, and that did operate, as a fraud and deceit upon Plaintiff.

58. The Columbia primary violators, and each of the, knew of the falsity of the representations described in paragraph 41 above, or recklessly failed to ascertain the truth of the representations. The Columbia primary violators knew of the omissions of material fact described in paragraph 43 above, or recklessly failed to disclose these facts.

59. Defendants Analysis, Hernandez, Chandler, Anico, LCI, Computer Value, Cuthbert, Rosen Associates, SSWPI, Rosen, TMS, and Turi (the "Columbia aiders and abettors") knew that their actions, as described in paragraphs 37b-f and 44 above, furthered and provided substantial assistance to the Columbia primary violators in committing a fraud on Plaintiff.

60. The Defendant primary violators' and aiders' and abettors' acts as described herein constitute a violation of Section 10 (b) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated thereunder, 15 U.S.C. § 78j (b), and 17 C.F.R. 240.10b-5.

61. As a result of these acts, Plaintiff is entitled to recover damages equal to all sums paid for his investment, together with interest thereon since the date paid.

* * *

IN THE UNITED STATES DISTRICT COURT
FOR THE DISTRICT OF OREGON

Civil No. 86-1368-RE

JOHN V. REITZ *et al.*,
Plaintiffs,

v.

LEASING CONSULTANTS ASSOCIATES, *et al.*,
Defendants.

Civil No. 86-1369-RE

JOHN and JANICE GILBERTSON, *et al.*,
Plaintiffs,

LEASING CONSULTANTS ASSOCIATES, *et al.*,
Defendants.

Civil No. 87-593-RE

ANTHONY E. CATALAN,
Plaintiff,

v.

PAULSON INVESTMENT COMPANY, INC.*et al.*,
Defendants.

U.S. DISTRICT COURT
DISTRICT OF OREGON

FILED

JUL 14 1988

BY ROBERT M. CHRIST, CLERK DEPUTY

Based on the record,

IT IS ORDERED that judgment is for defendants and these three cases are DISMISSED.

Dated this 14 day of July, 1988.

/s/ Robert M. Christ,

Robert M. Christ, Clerk
United States District Court
District of Oregon

FILED
DEC 5 1990
JOSEPH F. SPANIOL, JR.
CLERK

No. 90-333

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ, and ANTHONY CATALAN, *et al.*,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF FOR PETITIONER

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QUESTION PRESENTED

Whether private actions for damages, authorized by implication under § 10(b) of the Securities Exchange Act of 1934 (15 U.S.C. § 78j(b)) and Rule 10b-5 (17 C.F.R. § 240.10b-5) promulgated thereunder, should be governed by the uniform one and three year statutes of limitations applicable to express antifraud private causes of action created by the Securities Act of 1933 and the Securities Exchange Act of 1934 rather than by limitations periods derived from the laws of the various States.

LIST OF PARTIES

In addition to the respondents named in the caption, the following parties were appellants in the court below:

Clifford B. Alterman, John Ball, Ruth Beecher, Theodore Beecher, Carolyn Beecher, Walter L. Beers, Robert E. Boekenoogen, Charles W. Botsford, Robert Callahan, Bonnie J. Chambers as Conservator of the Estate of Robert W. Chambers, Joan Chatham, Ronald Chatham, Cliff Chulos, Perry Coleman, David Collier, Leo DePretto as Personal Representative of the Estate of Howard E. White, Arlyss D. Dunham, Jack E. Evans, Janice Gilbertson, Robert A. Graham, Harry E. Groth, Jr., William L. Gunnell, Woodrow Gwyn, Floyd E. Hambleton, Robert E. Johnson, Ronald Kirkilie, Judith MacDonald, Nickolas J. Madesh, Jerry E. Marks, H. Winston Marshall, Jay L. Maxwell, Maxwell McDonald Investments, David McCullam, James R. McDonald, Ward E. Moore, Ethel Nunemacher, Howard H. Overback, Elman Peterson, Jr., Dale R. Peterson, Joseph C. Player, Deane E. Reimann, Earl D. Riddle, Harlan C. Selby, Bruce Sigman, Edith Trykar, Theodore Trykar, C. Wayne Warren, R. Mattison White, Paul Winklesky, Larry G. Zettle.

In addition to petitioner, the following parties were appellees in the court below:

Alanthus Computer Corp., Alanthus Corp., Arnheim & McCostis, Anders G. Arnheim, Berlent Industries, Inc., Harvey N. Berlent, Buhler Software Services, Ronald Buhler, Comdisco, Inc., Computer Value Associates, John M. Costello, James B. Cuthbert, Jerrold Feingold, Leonard Feingold, Edward G. Fizell, Global Computer Corp., Mark A. Hanson, Richard A. Heitmeyer, Robert M. Hurwitz, Jeflen Consulting Corp., Ronald Johnson, Martin S. Karnoff, Robert M. Kirby, Kirby Microprocessors, Inc., Kirby Computer Systems, Inc., Leasing Consultants Associates, Leasing Consultants, Inc., David G. Marks, Richard M. McCostis, William L. McKenna, P-Stat, Inc., Martin D.

Pine, Kenneth M. Pontikes, Gordon S. Rosen Associates, Gordon S. Rosen, Noah Schreiber, Software Systems for Word Processors, Inc., Start Systems, Inc., Technical Marketing Services, Texcom Equipment Corp., Leonard F. Turi, William A. Ward, Robert A. Weber, Richard A. Wellbrock, Wayne Hamersly, Sherman Kellar, Mack, Roberts, Hoyle & Co., Roger Nelson, Paulson Investment Co., James D. Quenemoen, Rockwood Computer Corp., Michael Welwood, R. G. Williams.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-333

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ, and ANTHONY CATALAN, *et al.*,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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BRIEF FOR PETITIONER

OPINIONS BELOW

The February 5, 1990 memorandum decision of the United States Court of Appeals for the Ninth Circuit (Pet. App. 8a-18a), and the July 13, 1988 opinion of the United States District Court for the District of Oregon (Pet. App. 22a-43a) are not published.

JURISDICTION

The decision and judgment of the Court of Appeals (Pet. App. 8a-18a) were filed on February 5, 1990. A petition for rehearing with a suggestion for rehearing *en banc* was

denied on May 16, 1990. Pet. App. 19a-21a. The petition for writ of certiorari was timely filed on August 10, 1990. The petition was granted on October 9, 1990. This Court has jurisdiction over this case pursuant to 28 U.S.C. § 1254(1).

STATUTES, REGULATIONS AND RULES

This case principally involves the following statutes, regulations, and rules, which are set out verbatim in the Appendix to this Brief.

1. Sections 11(a)-(b), 12 and 13 of the Securities Act of 1933, 15 U.S.C. §§ 77k(a)-(b), 77*l* and 77m.

2. Sections 9(a)-(c), 9(e), 10(b), 16(b), 18(a), 18(c), 20A and 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78i(a)-(c), 78i(e), 78j(b), 78p(b), 78r(a), 78r(c), 78t-1 and 78cc(b).

3. Securities and Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5.

STATEMENT OF THE CASE

This case arises from the sale of what the plaintiffs below have characterized as "tax shelter limited partnerships." J.A. 17, 124. In 1979, 1980 and 1981, units in several separate Connecticut limited partnerships were offered to investors in Oregon and several other States. The partnerships were designed and promoted by various individuals and their related entities.[1]

Each limited partnership was described in an investment memorandum. Petitioner Lampf, Pleva, Lipkind, Prupis &

[1] The facts taken from the pleadings are presumed true for the purpose of the proceedings before this Court. The complaints alleged that the individual defendants who organized the partnerships were citizens of New Jersey and that their related entities included a New Jersey partnership and a Delaware corporation with its principal place of business in New Jersey. J.A. 22-23, 129, 231.

Petigrow ("Lampf") is a New Jersey law firm that allegedly prepared a "model offering memorandum" that served as the basis for the investment memoranda in most of the partnerships and also prepared tax opinions that appeared as exhibits to the investment memoranda for those partnerships. Each investment memorandum described transactions that would be made by the partnership consisting of the purchase and the leasing to others of certain computer equipment and software.[2]

The partnerships closed in 1979, 1980 and 1981. The last purchases by any investors involved in this case occurred in June 1981. J.A. 108, 210. During the succeeding years, the investors received periodic written reports regarding the partnerships' progress. *See* Pet. App. 31a. Without exception, the reports notified the limited partners that the partnerships were economic failures.

In 1986, after the Internal Revenue Service began to disallow the investors' tax benefits, a broker-dealer who had sold some of the partnership interests agreed to finance investors' lawsuits in exchange for a release from liability. Two suits were filed on November 3, 1986, in the United States District Court for the District of Oregon. J.A. 5, 9. A third suit was filed on June 4, 1987 in the same court. J.A. 14. All three suits alleged federal claims under § 10(b) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. § 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. § 240.10b-5 (the "§ 10(b) claims"); § 17(a) of the Securities Act of 1933 ("1933 Act"), 15 U.S.C.

[2] The investors have also sued the New York and New Jersey parties who sold the equipment to the partnerships (J.A. 23, 130, 231-32), the New York and Texas equipment appraisers identified in the investment memoranda (J.A. 25, 132, 233-34), the New York and New Jersey residents who appraised the software (J.A. 25-26, 132-33, 234), the equipment lessees, who were from Delaware, Illinois, New York, and North Carolina (J.A. 23-24, 130, 232), and software marketing companies from New York, New Jersey and Pennsylvania (J.A. 22-23, 129, 231).

§ 77q(a); and the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. §§ 1961-1968; as well as pendent state law claims.

The District Court consolidated the cases for discovery and ordered that discovery be limited initially to matters relevant to the statute of limitations. In February 1988, petitioner Lampf and other defendants moved for summary judgment on the grounds that the actions were not timely filed. On July 13, 1988, the District Court issued its opinion granting summary judgment in favor of defendants. *See* Pet. App. 22a-43a. The District Court did not address Lampf's argument that § 10(b) claims should be governed by a uniform federal statute of limitations. Instead, applying Oregon's two-year statute of limitations for fraud, the court held that the investors' § 10(b) claims were time-barred because they had failed to file suit within two years after they were put on "inquiry notice" of their potential claims. *See* Pet. App. 43a. The District Court dismissed all three cases. J.A. 253-54.[3]

The Ninth Circuit reversed, holding that there were issues of material fact relating to the investors' notice of their § 10(b) claims and the defendants' alleged fraudulent concealment of those claims. Pet. App. 10a, 16a. Like the District Court, the Ninth Circuit applied Oregon's two-year fraud limitations period and did not expressly address Lampf's argument that federal law should provide the limitations period for § 10(b) claims. Pet. App. 12a.

Lampf filed a timely petition for rehearing and suggestion for rehearing *en banc*, which was denied on May 16, 1990. On June 20, 1990, the Court of Appeals denied Lampf's motion for stay of issuance of the mandate. Lampf

[3] The District Court dismissed the claims brought under § 17(a) of the 1933 Act on the ground that § 17(a) does not create a private right of action. Pet. App. 34a. It also dismissed the RICO counts as untimely and declined to retain pendent jurisdiction over the state claims. Pet. App. 43a.

filed its petition for writ of certiorari on August 10, 1990, and the petition was granted on October 9, 1990.

If, as determined by the Court of Appeals, the Oregon statute of limitations is applicable to the § 10(b) claims in this case, litigation will continue in the District Court over when the plaintiffs' claims were discovered. If, on the other hand, the statute of limitations applied to this case is drawn from the federal securities laws as urged by petitioner, the claims will be time-barred.

SUMMARY OF ARGUMENT

This case presents a clear and compelling choice for the Court: should private civil actions for damages authorized by implication under § 10(b) of the Securities Exchange Act of 1934 and Securities and Exchange Commission Rule 10b-5 ("§ 10(b) cases") be governed (1) by statutes of limitations selected individually on a case-by-case, plaintiff-by-plaintiff basis from the myriad of potential laws found in the statutes of fifty States, or (2) by the specific limitations period explicitly selected by Congress to govern the "comparable express causes of action" (*Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 736 (1975)) that it created at the same time that it enacted § 10(b)?

This Court has determined that, " '[f]ew areas of the law stand in greater need of firmly defined, easily applied rules than does the subject of periods of limitations.' " *Wilson* v. *Garcia*, 471 U.S. 261, 266 (1985) (quoting *Chardon* v. *Dumaro Soto*, 462 U.S. 650, 667 (1983) (Rehnquist, J., dissenting)). Yet the existing practice of borrowing state limitations periods in § 10(b) cases pulls in the opposite direction. Indeed, it is such a "nightmare" that "[w]ith a unanimity unmatched in any other corner of securities law, *everyone* wants a simpler way—and to everyone that means a uniform federal statute of limitations." *Short* v. *Belleville Shoe Manufacturing Co.*, 908 F.2d 1385, 1389 (7th Cir. 1990) (emphasis added), *cert. pending* (No. 90-526). This case offers the Court the opportunity to adopt for § 10(b)

actions the limitations period embraced by Congress for the principal nonderivative counterparts to § 10(b) and thereby to eliminate the chaos that has overtaken and threatens the effectiveness of private § 10(b) actions.

The Securities Act of 1933 and the Securities Exchange Act of 1934 "constitute interrelated components" (*Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 206 (1976)) of the comprehensive national regime enacted by the Seventy-Third Congress to regulate the interstate marketing of securities. These two laws contain several express prohibitions of misleading and deceptive practices in the marketing of securities and establish explicit private rights of action for violations of these provisions. Section 10(b) of the 1934 Act was intended to supplement these provisions; to be a "catch-all" to enable the newly created Securities and Exchange Commission to prohibit new and innovative manipulative devices and schemes not explicitly addressed in the two Acts. While § 10(b) did not expressly create a private right of action, the courts soon discerned one and the implied § 10(b) action is now an accepted constituent of the national securities enforcement scheme.

The problem presented by this case arose because, in the absence of an explicit federal statute of limitations for § 10(b) cases, the federal courts applying the § 10(b) right of action turned almost uniformly to state laws as the source of limitations periods to govern those actions. But this practice has resulted in confusion, inefficiency, inconsistency, unpredictability, delay and forum shopping. Each State has one or more limitations period for fraud, securities law violations, contract claims or other transgressions that might serve as a limitations period for a § 10(b) claim. A federal court grappling with a typical § 10(b) claim, which is invariably multistate in nature and is often a class action involving plaintiffs and defendants from many States, must select a suitable limitations period for

each individual claim. The consequence has been a complete lack of consistency. The process has been complicated exponentially by the application of different state and federal tolling periods, changes in state laws, and different analyses by federal judges throughout the Nation. Results vary from circuit to circuit, state to state, district to district and even from plaintiff to plaintiff within a particular case. Plaintiffs seek out the forum with the most felicitous limitations period, and the courts and litigants spend vast resources resolving disputes over the appropriate statute to apply.

The problems created by applying numerous potential state limitations periods to § 10(b) claims have become intolerable. "Never has the process been more enervating than in securities law . . . . [T]he courts of appeals disagree on every possible question about limitations periods in securities cases. Only Congress or the Supreme Court can bring uniformity to this field . . . ." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), *cert. denied*, 484 U.S. 943 (1987).

Fortunately, the Court has made clear in its recent jurisprudence that no statute and no pronouncement of this Court compels the chaos that has come to characterize the limitations-period phase of § 10(b) litigation. In *DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151 (1983), and *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), the Court flatly rejected the notion that federal courts must always apply the most analogous state statute of limitations to federally created rights when the statute creating those rights is silent on the proper limitations period. Instead, the task is to " 'borrow' " "the most suitable statute." *DelCostello*, 462 U.S., at 158. While state law may often supply that analogy, state statutes may be particularly unsatisfactory vehicles for the enforcement of federally created rights if "all claims arising out of the federal statute 'should be characterized in the same way' " for limitations period purposes rather

than " 'differently depending upon the varying factual circumstances and legal theories presented in each individual case.' " *Agency Holding Corp.*, 483 U.S., at 147 (quoting *Wilson* v. *Garcia*, 471 U.S., at 268). In those instances, " 'it may be inappropriate to conclude that Congress would choose to adopt state rules at odds with the purpose or operation of federal substantive law.' " *Agency Holding Corp.*, 483 U.S., at 147 (quoting *DelCostello*, 462 U.S., at 161). If a federal law provides " 'a closer analogy' " than state statutes, and if " 'the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking,' " the Court has " 'not hesitated' " to select the federal standard. *Agency Holding Corp.*, 483 U.S., at 148 (quoting *DelCostello*, 462 U.S., at 171-72).

Selecting a federal limitations period is particularly appropriate where the right of action is implied by the courts from a federal regulatory scheme that does contain a limitations period for comparable express rights of action, in contrast to a situation involving an express federal right of action for which Congress affirmatively chose not to enact a limitations period.

Section 10(b) presents a paradigmatic context for applying the standard articulated in *DelCostello* and *Agency Holding Corp.* to recognize a federal limitations period for implied federal rights of action being litigated in federal courts. Section 10(b) cases involve rights derived from a federal statute, are litigated exclusively in federal courts pursuant to federal rules of evidence, and are inevitably multistate in nature. These cases may arise in an infinite variety of contexts and present an unlimited array of factual circumstances. It is flatly inconsistent with the concept of a uniform national scheme of securities regulation for these cases to be litigated to different conclusions depending upon the accident of the location of the particular federal forum in which they are presented. *Cf. Reves* v. *Ernst & Young*, 110 S. Ct. 945, 954 (1990). Congress ordained a cohesive and comprehensive regulatory regime for securities laws, not a potpourri of inconsistent, conflicting and confusing regulations that encourage vexatious litigation and spawn uncertainty in the marketplace. *See Blue Chip Stamps*, 421 U.S., at 739-41.

There can be no doubt that the Congress that adopted § 10(b) would have chosen for § 10(b) actions the same federal limitations period that it debated and embraced for the "comparable express" (*id.*, at 736) private antifraud remedies it created simultaneously rather than the uncertain, variable and constantly changing array of state limitations periods. No goal is served by requiring courts to distinguish between the different factual and legal contexts in which § 10(b) cases may arise. In fact, the confusion and the waste of judicial and private resources generated by this existing system undermine severely not just the congressional goals that motivated § 10(b) but also the fundamental purposes of uniformity and consistency that underlie both the 1933 and 1934 Acts.

The standards articulated by the Court in *DelCostello* and *Agency Holding Corp.* lead inexorably to the conclusion that there is a " 'federal law [that] clearly provides a closer analogy than available state statutes'." *Agency Holding Corp.*, 483 U.S., at 148 (quoting *DelCostello*, 462 U.S., at 171-72). And the "federal policies at stake and the practicalities of litigation make that rule" not simply "a significantly more appropriate vehicle for interstitial lawmaking" but the *only* rule for § 10(b) that reflects Congress' considered judgment concerning the balance to be struck between the interests of defrauded investors and the importance to the investment community and the national economy of certainty, stability and repose.

The private rights of action for securities fraud expressly created in §§ 11 and 12 of the 1933 Act and §§ 9, 18 and 29 of the 1934 Act must all be initiated within one year of discovery but no later than three years after the violation. Congress not only debated the wisdom of

the length of these limitations periods, but it tellingly overrode its initial decision to adopt a two-year/ten-year standard for 1933 Act violations in order to embrace the same one-year/three-year standard for the 1933 Act that it applied to the antifraud provisions of the 1934 Act, thus implementing a uniform standard for both Acts.

There are no other suitable alternatives. The 1933 and 1934 Acts contain only two other statutes of limitations. The two-year limitations period applicable to recoveries of profits on short-swing sales under § 16(b) of the 1934 Act has no discernible relationship to § 10(b) actions. The five-year limitations period of §20A of the 1934 Act, enacted as part of the Insider Trading and Securities Fraud Enforcement Act of 1988 ("ITSFEA"), is equally inappropriate. It is a narrow remedy created to respond to a limited insider trading problem. It was enacted five decades after § 10(b) and was not intended to apply generically to securities fraud. Neither the text of the ITSFEA nor its legislative history reflects any understanding or intention that its limitations period would apply to the broad range of § 10(b) cases. In fact, it was made expressly *inapplicable* to the right to bring any action "implied from a provision" of the 1934 Act. Applying the ITSFEA's five-year limitations period to § 10(b) actions would encourage claimants under §§ 11 and 12 of the 1933 Act and §§ 9, 18 and 29 of the 1934 Act to recharacterize their complaints as § 10(b) actions in order to take advantage of the longer limitations period, thus nullifying the careful congressional standard explicitly adopted to govern those provisions. "It would indeed be anomalous to impute to Congress an intention to expand the plaintiff class for a judicially implied cause of action beyond the bounds it delineated for comparable express causes of action." *Blue Chip Stamps*, 421 U.S., at 736.

The one-year/three-year limitations period in the 1933 and 1934 Acts is the perfect standard for application to § 10(b) cases. It effectuates the federal policies behind

§ 10(b) and the federal securities laws generally and its application would alleviate a serious problem affecting the practicalities of § 10(b) litigation that does inestimable damage to litigants and to the courts.

ARGUMENT

I

CONGRESS ENACTED THE SECURITIES ACT OF 1933 AND THE SECURITIES EXCHANGE ACT OF 1934 IN ORDER TO ESTABLISH A UNIFORM NATIONAL SYSTEM FOR THE REGULATION OF INTERSTATE COMMERCE IN SECURITIES

In response to the stock market crash of 1929, "Congress enacted two landmark statutes regulating securities." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 727 (1975). The Securities Act of 1933, 15 U.S.C. §§ 77a, *et seq.*, generally regulates the initial distribution of securities in interstate commerce and was intended to promote orderly, efficient formation of capital, and to "provide investors with full disclosure of material information," thereby protecting them from fraud. *See Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 195 (1976).[4] The Securities Exchange Act of 1934, 15 U.S.C. §§ 78a, *et seq.*, was also intended to bring stability and order to the securities markets, while at the same time protecting investors from "manipulation of stock prices" and other fraudulent practices "through regulation of transactions on

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[4] The history of the 1933 Act indicates that the purpose of that legislation was "to protect [both] the investing public and honest business." S. Rep. No. 47, 73d Cong., 1st Sess. 1 (1933), *reprinted in* 2 J. Ellenberger & E. Mahar, *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934* Item 17 (1973); 77 Cong. Rec. 2983 (May 8, 1933) (statement of Sen. Fletcher); *see also* 77 Cong. Rec. 937 (Mar. 29, 1933) (letter from President Roosevelt to Congress) ("The purpose of the legislation I suggest is to protect the public with the least possible interference to honest business").

securities exchanges and in over-the-counter markets." *Ernst & Ernst*, 425 U.S., at 195; *see also United States* v. *Naftalin*, 441 U.S. 768, 774-76 (1979) (discussing dual purposes of the securities acts).[5] Section 4 of the 1934 Act created the Securities and Exchange Commission ("Commission") to administer and enforce the federal securities laws. 15 U.S.C. § 78d. In addition to rulemaking and quasi-judicial authority, the Commission has "an arsenal of flexible enforcement powers." *Ernst & Ernst*, 425 U.S., at 195.

The 1933 and 1934 Acts responded to the inadequacy and inconsistency of state securities statutes[6] by establishing a comprehensive federal framework for the regulation of securities markets and transactions. These sweeping statutes reflected Congress' understanding that the health and integrity of securities markets were matters of national importance requiring uniform treatment through federal legislation. Indeed, in § 2 of the 1934 Act, *see* 15 U.S.C. § 78b, Congress explained that it was motivated by the conviction that "transactions in securities . . . are affected with a *national* public interest . . . ." (emphasis added).

The 1933 and 1934 Acts contain several express private remedies that permit individuals to sue for losses resulting from untruthful or misleading communications and manipulative, fraudulent and deceptive conduct in connection with securities transactions. For example, §§ 11 and 12(2)

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[5] As the House report pointed out, the 1934 Act was an attempt "to save, not destroy, stock markets and business, by making necessary changes in time." H.R. Rep. No. 1383, 73d Cong., 2d Sess. 3 (1934), *reprinted in* 5 J. Ellenberger & E. Mahar, *supra* note 4, at Item 18.

[6] I L. Loss & J. Seligman, *Securities Regulation* 227-28 (3d ed. 1989). Prior to the enactment of the 1933 and 1934 Acts, securities transactions were governed only by state laws, which varied significantly from jurisdiction to jurisdiction. *Id.*

of the 1933 Act, 15 U.S.C. §§ 77k, 77*l*(2), permit actions for false or misleading statements or omissions in registration statements and prospectuses. Similarly, § 9(e) of the 1934 Act, 15 U.S.C. § 78i(e), creates a private right of action for false or misleading statements and manipulative conduct in connection with securities registered on a national exchange. Section 18(a) of the 1934 Act, 15 U.S.C. §78r(a), permits investors to sue for false or misleading statements "in any application, report, or document" filed with the Commission. And § 29(b) of the 1934 Act, 15 U.S.C. § 78cc(b), was amended in 1938 to permit private actions to void certain purchase or sale contracts that violate the statute or rules promulgated thereunder.[7]

When Congress created these express private rights of action for the victims of fraudulent practices, it engaged in extensive debate and deliberation regarding the appropriate corresponding statutes of limitations.[8] The 1934 Act made claims under §§ 11 and 12 of the 1933 Act and §§ 9 and 18 of the 1934 Act all subject to the same limitations period: one year from discovery of the facts constituting the violation and in no event more than three years after the violation (or transaction) occurred.[9]

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[7] Another private right of action is expressly authorized by § 16(b) of the 1934 Act, 15 U.S.C. § 78p(b), which allows a shareholder to recover, on behalf of the corporation, "short-swing profits," *i.e.*, the profits made by certain insiders who have purchased and sold shares within a six-month period. In the 1988 ITSFEA legislation, Congress amended the 1934 Act to add § 20A, 15 U.S.C. § 78t-1, to create a remedy in favor of "contemporaneous traders" against persons who violate other provisions of the securities laws by trading while in possession of material, nonpublic information.

[8] *See infra* pages 37-41.

[9] As will be discussed in greater detail, *infra*, most claims under §§ 11 and 12 of the 1933 Act were originally required to be filed within two years from discovery of the untrue statement but no later than ten years after the security was offered to the public. When it passed the 1934 Act, Congress reconsidered the two-year/ten-year provision

The principal additional provision of the securities laws that addresses fraudulent and deceptive conduct is § 10(b) of the 1934 Act, 15 U.S.C. § 78j(b).[10] Section 10(b) makes it "unlawful" to

> use or employ, in connection with the purchase or sale of any security . . . any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

15 U.S.C. § 78j(b). As this Court has recognized, § 10(b) was "described rightly" by its drafters "as a 'catchall clause to enable the Commission to deal with new manipulative [or cunning] devices.' " *Ernst & Ernst*, 425 U.S., at 203 (citation omitted).

Pursuant to the statutory authority conferred by § 10(b), the Commission in 1942 promulgated Rule 10b-5, 17 C.F.R. § 240.10b-5. It broadly prohibits fraudulent schemes and material misstatements or omissions in connection with the purchase or sale of securities.[11]

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and established a uniform one-year/three-year limitations period for private actions under the antifraud provisions of both the 1933 and 1934 Acts. In 1938, a one-year/three-year statute of limitations was adopted for § 29(b) of the 1934 Act. *See* 1934 Act, § 29(b), 15 U.S.C. § 78cc(b).

The only deviations from the one-year/three-year rule are a two-year statute of limitations contained in § 16 on actions to recover short-swing profits and a five-year limitations period in § 20A relating to actions by contemporaneous traders under the ITSFEA.

[10] *See also* 1933 Act, § 17, 15 U.S.C. § 77q; 1934 Act, § 14(e), 15 U.S.C. § 78n(e).

[11] Rule 10b-5 provides:

> It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
>
> (a) To employ any device, scheme, or artifice to defraud,
>
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or
>
> (c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

Neither § 10(b) nor Rule 10b-5 explicitly established a private right of action. However, to complement the "numerous carefully drawn express civil remedies" of the two securities acts, *Blue Chip Stamps*, 421 U.S., at 730, the courts inferred a private remedy under § 10(b) and Rule 10b-5. *See, e.g., Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512, 514 (E.D. Pa. 1946). This Court subsequently confirmed the existence of such an implied right of action. *See, e.g., Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 380 (1983).

Because Congress had not expressly created a private right of action for § 10(b) violations, it did not expressly enact any limitations period applicable to such actions. Until recently, the federal courts have uniformly applied varying state statutes of limitations to § 10(b) claims, rather than a limitations period drawn from § 10(b)'s express counterparts in the 1933 and 1934 Acts. *Ernst & Ernst*, 425 U.S., at 210 n.29.

II

SECTION 10(b) CLAIMS SHOULD BE SUBJECT TO A UNIFORM FEDERAL STATUTE OF LIMITATIONS

A. Standards for Choosing a Limitations Period for a Federal Right of Action.

This Court has long recognized that statutes of limitations are "vital to the welfare of society and are favored

in the law," because "they promote repose by giving security and stability to human affairs." *Wood* v. *Carpenter*, 101 U.S. 135, 139 (1879); *see also McCluney* v. *Silliman*, 3 Pet. (28 U.S.) 269, 277 (1830) (limitations periods "tend to the peace and welfare of society"). Statutes of limitations are intended to promote "fairness to defendants" and to preclude litigation of "stale claims." *Burnett* v. *New York Central Railway Co.*, 380 U.S. 424, 428 (1965).[12]

However, not all federal rights of action are governed by an explicit federal statute of limitations. In creating express private rights of action, Congress sometimes is silent with respect to the appropriate limitations period, *see, e.g., Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S. 143, 146 (1987), or, as is the case here, the courts sometimes infer private rights of action from federal statutes that do not expressly provide for a private remedy and therefore do not necessarily include a limitations period. In such situations, the Court has "borrowed"[13] a statute of limitations "from some other source," *DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151, 158 (1983), rather than impose no limitations period at all. *Agency Holding Corp.*, 483 U.S., at 156; *see also Wilson*, 471 U.S., at 271 (a "federal cause

[12] *See also Johnson* v. *Railway Express Agency, Inc.*, 421 U.S. 454, 463-64 (1975) (limitations periods "inevitably reflect[] a value judgment concerning the point at which the interests in favor of protecting valid claims are outweighed by the interests in prohibiting the prosecution of stale ones"). As the Court has observed, "[j]ust determinations of fact cannot be made when, because of the passage of time, the memories of witnesses have faded or evidence is lost." *Wilson* v. *Garcia*, 471 U.S. 261, 271 (1985).

[13] Various labels have been used to describe the practice of selecting state statutes of limitations to apply to federal claims. The term "borrowing" may not be accepted universally as an apt characterization of the practice. *See Agency Holding Corp.*, 483 U.S., at 158 (Scalia, J., concurring in the judgment). The practice also has been referred to as "absorption" of state law. *See, e.g., Holmberg* v. *Armbrecht*, 327 U.S. 392, 395 (1946).

of action 'brought at any distance of time' would be 'utterly repugnant to the genius of our laws' ") (quoting *Adams* v. *Woods*, 2 Cranch (6 U.S.) 336, 341 (1805)).[14]

Although historically "courts have generally looked to [state] law as the source" of limitations periods for federal remedies when federal law is silent on the question, *American Pipe & Construction Co. v. Utah*, 414 U.S. 538, 557 (1974), in 1983 in *DelCostello* and four years later in *Agency Holding Corp.* the Court examined the standards for choosing an appropriate limitations period and categorically rejected the suggestion that "federal courts always should apply the state statute of limitations most analogous to each individual case whenever a federal statute is silent on the proper limitations period." *Agency Holding Corp.*, 483 U.S., at 146; *see also Reed* v. *United Transportation Union*, 109 S. Ct. 621 (1989). Neither the Rules of Decision Act, 28 U.S.C. 1652,[15] nor any other aspect of federal law *requires* reference to state law, *DelCostello*, 462 U.S., at 159 n.13, and "[i]n some circumstances . . . state statutes of limitations can be unsatisfactory vehicles for the enforcement of federal law," *id.*, at 161.

Indeed, "[s]tate legislatures do not devise their limitations periods with national interests in mind, and it is the

[14] *But see Holmberg*, 327 U.S., at 395 (declining to apply any statute of limitations to federal equitable claims, instead invoking laches doctrine).

[15] The Rules of Decision Act provides that state law shall be regarded as providing the rules of decision when federal law does not "otherwise require or provide." 28 U.S.C. § 1652. The Court in *DelCostello* concluded that the "choice of a limitations period for a federal cause of action is itself a question of federal law. If the answer to that question . . . is that a timeliness rule drawn from elsewhere in federal law should be applied, then the Rules of Decision Act is inapplicable by its own terms." 462 U.S., at 159 n.13; *see also id.*, at 174 n.1 (O'Connor, J., dissenting) (the Rules of Decision Act "only puts the question, for it simply requires application of state law unless federal law applies"); *cf. Agency Holding Corp.*, 483 U.S., at 162 (Scalia, J., concurring in the judgment).

duty of the federal courts to assure that the importation of state law will not frustrate or interfere with the implementation of national policies." *Occidental Life Insurance Co.* v. *EEOC*, 432 U.S. 355, 367 (1977) (EEOC civil rights enforcement actions are subject only to time limitations expressly contained in Title VII and federal equitable principles); *see also McAllister* v. *Magnolia Petroleum Co.*, 357 U.S. 221, 224-26 (1958) (applying federal limitations period to judicially created maritime rights); *Holmberg*, 327 U.S., at 395 (federal principles of laches, rather than state limitations periods, apply to enforce federal equitable rights).

The Court's decisions in *DelCostello* and *Agency Holding Corp.*, which rejected state limitations periods in favor of federal analogs, identified several factors that should be considered in selecting the most appropriate statute of limitations for an implied federal right of action. One factor is whether all claims arising out of the federal statute " 'should be characterized in the same way' " for statute of limitations purposes, " 'or whether they should be evaluated differently depending upon the varying factual circumstances and legal theories presented in each individual case.' " *Agency Holding Corp.*, 483 U.S., at 147 (quoting *Wilson v. Garcia*, 471 U.S., at 268). If so, "a uniform statute of limitations is required to avoid intolerable 'uncertainty and time-consuming litigation.' " *Id.*, at 150 (quoting *Wilson*, 471 U.S., at 272). In addition, it must be determined whether a rule from elsewhere in federal law provides a closer analogy than available state statutes, and, if so, whether the " 'federal policies at stake and the practicalities of litigation" make that federal rule "a significantly more appropriate vehicle for interstitial lawmaking . . . .' " *Id.*, at 148 (quoting *DelCostello*, 462 U.S., at 172).

The Court in *DelCostello* also declared that "it makes more sense" to assume that Congress intended application of a state limitations period "to a cause of action expressly created by Congress than . . . to one found by the courts

to be implied in a general statutory scheme—especially when that general statutory scheme itself contains a federal statute of limitations for a related but separate form of relief." 462 U.S., at 159 n.12. If Congress created an express right, but did not adopt an express limitations period for that right, it might be assumed that Congress intended that courts implementing that right follow the practice of turning to state law. The same cannot be said when the right itself is implied from a federal statute and was not expressly created by Congress. Thus, although the Court did not reach the question in *DelCostello*, it seemed to embrace the logic that there is considerably less justification for resorting to state limitations periods when an implied right of action is involved and the federal statutory scheme includes an express limitations period for comparable remedies.[16]

B. The Prevailing Practice of Borrowing State Statutes of Limitations for § 10(b) Claims Has Resulted in Inconsistency, Unpredictability, Delay, Heightened Expense and Forum Shopping—Frustrating the Policies Underlying the Securities Acts.

1. The Federal Courts Currently Apply a Multitude of Widely Varying and Poorly Suited State Limitations Periods to § 10(b) Claims.

Section 10(b) claims are litigated exclusively in federal courts. 1934 Act, § 27, 15 U.S.C. § 78aa. Nonetheless, the

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[16] *See also United Parcel Service, Inc.* v. *Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring in the judgment) ("the fact that Congress did not provide a limitations period for a judicially enforceable action later found implied in the NLRA is not comparable to a congressional failure to establish a time limitation for an action it expressly creates by statute . . . . [I]t cannot reasonably be assumed . . . that congressional silence reflects an intent to apply state statutes of limitation for an action based in part on rights and obligations traceable to the NLRA."); *McAllister*, 357 U.S., at 228-29 (Brennan, J., concurring).

first courts to consider what limitations period to apply to § 10(b) claims borrowed the most analogous law of the forum State, *see Fischman* v. *Raytheon Manufacturing Co.*, 188 F.2d 783, 787 (2d Cir. 1951); *Osborne* v. *Mallory*, 86 F. Supp. 869, 879 (S.D.N.Y. 1949), establishing a practice that persisted for more than 40 years.[17] Different federal courts implemented the process differently. Even respondents candidly acknowledged in opposition to the petition that the result was at least "fifty different rules creating differences within and between circuits." Respondents' Opp. to Pet. for Cert., at 2. That figure, however, understates the magnitude of the problem.

The confusion that has resulted from applying varying state statutes of limitations to § 10(b) claims stems in part from the fact that such claims " 'encompass numerous and diverse topics and subtopics,' " *Agency Holding Corp.*, 483 U.S., at 146 (discussing civil RICO claims) (citation omitted), and, accordingly, "embrace a galaxy of actions," *In re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1543 (3d Cir.) (*en banc*), *cert. denied*, 488 U.S. 849 (1988). Section 10(b) claims "can be brought by a purchaser or seller of '*any* security' against '*any* person' who has used '*any* manipulative or deceptive device or contrivance.' " *Herman & MacLean*, 459 U.S., at 382 (emphasis in original) (quoting § 10(b)). A private party can bring a § 10(b) claim against, *inter alia*, persons who engage in manipulation of securities prices,[18] an issuer of securities who makes false or misleading statements,[19] lawyers and

[17] In *Ernst & Ernst*, 425 U.S., at 196 & n.2, and *Herman & MacLean*, 459 U.S., at 384 n.18, this Court took note of the fact that the lower courts looked to state law for a limitations period under § 10(b). The propriety of that practice was not a question presented in either case.

[18] *See Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 303 (1985); McLucas & Angotti, *Market Manipulation*, 22 Sec. & Commodities Reg. 103 (1989).

[19] *See Basic, Inc.* v. *Levinson*, 485 U.S. 224 (1988).

accountants who participate in securities offerings,[20] broker-dealers who commit fraud,[21] and certain fiduciaries who trade in the securities markets on the basis of material, nonpublic information.[22] Consequently, § 10(b) and Rule 10b-5 "may well be the most litigated provisions in the federal securities laws." *SEC* v. *National Securities, Inc.*, 393 U.S. 453, 465 (1969).

In searching for a suitable state law analog for § 10(b) cases, some courts, like the Ninth Circuit, have turned to the state statutes of limitations for common law fraud, while others have looked to state "blue sky" statutes regulating securities,[23] general personal injury statutes[24] and "catch-all" limitations periods.[25] Section 10(b) claims also could theoretically be compared to breach of contract claims, a variety of business torts, and breach of fiduciary duty actions.

However, no single state law right of action provides a satisfactory analog for § 10(b) claims even within one State. This Court has often rejected the contention that § 10(b) claims are analogous to common law claims for fraud and deceit: "[T]he typical fact situation in which the classic tort of misrepresentation and deceit evolved was light years away from the world of commercial transactions to which Rule 10b-5 is applicable." *Blue Chip Stamps*, 421 U.S., at 744-45; *accord Basic, Inc.* v. *Levinson*, 485 U.S. at 243-44 ("The modern securities markets, literally involving mil-

[20] *See Herman & MacLean*, 459 U.S., at 378.

[21] *See Bateman Eichler, Hill Richards, Inc.*, 472 U.S., at 301-03.

[22] *See Dirks* v. *SEC*, 463 U.S. 646, 653-54, 660-64 (1983).

[23] *See, e.g., Smith* v. *Duff & Phelps, Inc.*, 891 F.2d 1567 (11th Cir. 1990).

[24] *See, e.g., Maggio* v. *Gerard Freezer & Ice Co.*, 824 F.2d 123 (1st Cir. 1987).

[25] *See, e.g., Cunha* v. *Ward Foods, Inc.*, 501 F. Supp. 830, 837 (D. Haw. 1980).

lions of shares changing hands daily, differ from the face-to-face transactions contemplated by early fraud cases.").

In fact, Rule 10b-5 was promulgated in order to "rectify perceived deficiencies in the available common-law protections by establishing higher standards of conduct in the securities industry." *Herman & MacLean*, 459 U.S., at 389. Accordingly, § 10(b) claims differ from typical common law fraud claims in many important respects. *See Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 153-54 (1972) (reliance presumed in § 10(b) cases involving material omissions); *Herman & MacLean*, 459 U.S., at 390 (§ 10(b) claims, unlike actions for common law fraud, need not be proved by clear and convincing evidence); *Basic, Inc.*, 485 U.S., at 247 (discussing "fraud-on-the-market" theory and creating rebuttable presumption of reliance on public material misrepresentation in § 10(b) cases). For all these reasons, "[i]t is therefore clear that, far from being a mirror image or a reasonable facsimile of common law fraud, actions brought under section 10(b) and Rule 10b-5 appear to be *sui generis*." *Data Access*, 843 F.2d, at 1545.

State blue sky statutes also provide an unsatisfactory analogy to § 10(b). Blue sky statutes come in many forms, some of which bear little resemblance to § 10(b). *See generally* L. Loss, *Fundamentals of Securities Regulation* 877-78 (2d ed. 1988). In contrast to § 10(b), some blue sky laws may not impose any scienter or reliance requirements, *see Wood* v. *Combustion Engineering*, 643 F.2d 339, 345-46 (5th Cir. 1981), or may not permit sellers of securities, as opposed to purchasers, to sue for fraud, *see Data Access*, 843 F.2d, at 1544. Blue sky laws also may limit relief to rescission damages and preclude actions against "the attorneys and accountants of a corporate seller of securities." *See id.*[26]

[26] Other common claims under § 10(b) may be precluded as a matter of law under the state securities acts. *See, e.g. Nesbit* v. *McNeil*, 896 F.2d 380, 387 (9th Cir. 1990) (Oregon's blue sky statute does not provide a remedy for claims arising from a principal-agent transaction such as relationships between broker-dealers and their clients); *Biggans* v. *Bache Halsey Stuart Shields, Inc.*, 638 F.2d 605 (3d Cir. 1980) (Pennsylvania's blue sky statute does not recognize so-called "churning" claims in which a broker-dealer generates excessive and improper commissions).

Judge Easterbrook has described the difficulties and judicial costs in attempting to match state law to § 10(b) claims:

> Deciding which features of state periods of limitation to adopt for which federal statutes wastes untold hours. *Never has the process been more enervating than in securities law.* There are many potentially analogous state statutes, with variations for different kinds of securities offenses and different circumstances that might toll the period of limitations. Both the bar and scholars have found the subject vexing and have pleaded, with a unanimity rare in the law, for help.

Norris v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.) (emphasis added) (citations omitted), *cert. denied*, 484 U.S. 943 (1987); *see also Short* v. *Belleville Shoe Manufacturing Co.*, 908 F.2d 1385, 1389 (7th Cir. 1990) ("Lawyers and courts alike devote untold hours to identifying proper state analogies."), *cert. pending* (No. 90-526); *Friedlander* v. *Troutman, Sanders, Lockerman & Ashmore*, 788 F.2d 1500, 1504 (11th Cir. 1986) (rejecting case-by-case selection of analogy); *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 461 (3d Cir. 1979) (Seitz, J., dissenting) (discussing confusion and difficulties of matching § 10(b) claims to state law actions and observing that precedent is of little value in conducting such an inquiry).

The lengths of the limitations periods borrowed from state law by the federal courts have varied radically from

one jurisdiction to another, ranging from one year in Maryland, *see, e.g., O'Hara* v. *Kovens*, 625 F.2d 15, 18 (4th Cir. 1980), *cert. denied*, 449 U.S. 1124 (1981), to ten years in one court, *see Denny* v. *Performance Systems, Inc.*, Fed. Sec. L. Rep. (CCH) ¶ 93,387, at 91,981 (M.D. Tenn. Nov. 5, 1971).[27] Currently, federal courts in fourteen States, the District of Columbia, and Puerto Rico apply a two-year statute of limitations.[28] Nine States apply limitations pe-

[27] The ten-year Tennessee fraud limitations period borrowed in *Denny* has since been shortened to three years by amendment. *See Media General, Inc.* v. *Tanner*, 625 F. Supp. 237, 245-47 (E.D. Tenn. 1988).

[28] These jurisdictions are Alabama, the District of Columbia, Florida, Georgia, Iowa, Kansas, Louisiana, Maine, Mississippi, Missouri, Montana, North Carolina, Oklahoma, Oregon, Puerto Rico, and Virginia. *See, e.g., Smith* v. *Duff & Phelps, Inc.*, 891 F.2d 1567, 1570 (11th Cir. 1990) (Alabama blue sky law); *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411, 413 (D.C. Cir. 1977) (District of Columbia blue sky law); *Nortek, Inc.* v. *Alexander Grant & Co.*, 532 F.2d 1013, 1015 (5th Cir. 1976) (Florida blue sky law), *cert. denied*, 429 U.S. 1042 (1977); *Friedlander* v. *Troutman, Sanders, Lockerman & Ashmore*, 788 F.2d 1500, 1507 (11th Cir. 1986) (Georgia Securities Act); *In re Alodex Corp. Sec. Litig.*, 533 F.2d 372, 374 (8th Cir. 1976) (Iowa blue sky law); *Woods* v. *Homes & Structures of Pittsburgh, Kan., Inc.*, 489 F. Supp. 1270, 1284 (D. Kan. 1980) (Kansas fraud); *Davis* v. *A.G. Edwards & Sons, Inc.*, 635 F. Supp. 707, 715 (W.D. La. 1986) (Louisiana blue sky law), *modified*, 823 F.2d 105 (5th Cir. 1987); *Dyer* v. *Eastern Trust & Banking Co.*, 336 F. Supp. 890, 906 (D. Me. 1971) (Maine blue sky law); *Stewart* v. *Germany*, 631 F. Supp. 236, 247 (S.D. Miss. 1986) (Mississippi blue sky law); *Harris* v. *Union Elec. Co.*, 787 F.2d 355, 360 (8th Cir.) (Missouri blue sky law), *cert. denied*, 479 U.S. 823 (1986); *Volk* v. *D.A. Davidson & Co.*, 816 F.2d 1406, 1412 (9th Cir. 1987) (Montana fraud); *Umstead* v. *Durham Hosiery Mills, Inc.*, 578 F. Supp. 342, 347 (M.D.N.C. 1984) (North Carolina blue sky law); *Buford White Lumber Co. Profit Sharing & Sav. Plan & Trust* v. *Octagon Properties, Ltd.*, 740 F. Supp. 1553, 1567 (W.D. Okl. 1989) (Oklahoma fraud); *Williams* v. *Sinclair*, 529 F.2d 1383, 1387 (9th Cir. 1975) (Oregon fraud); *Rodriguez* v. *Banco Central*, 727 F. Supp. 759, 767 (D. P.R. 1989) (Puerto Rico blue sky law); *Land* v. *Dean Witter Reynolds, Inc.*, 617 F. Supp. 52, 53 (E.D. Va. 1985) (Virginia blue sky law).

Although no Alaska federal court has addressed this issue, a two-

riods of three years.[29] Federal courts in two States set their limitations periods at four years;[30] courts in two other States have used five years;[31] and four jurisdictions currently apply six-year statutes of limitations.[32]

year limitations period has been applied to a § 10(b) action arising in that State. *See Robertson* v. *Seidman & Seidman*, 609 F.2d 583, 586 (2d Cir. 1979) (applying Alaska personal injury limitations period).

[29] These States are Arizona, California, Colorado, Kentucky, Minnesota, South Carolina, Utah, Washington and West Virginia. *See, e.g., Semegen* v. *Weidner*, 780 F.2d 727, 733 (9th Cir. 1985) (Arizona fraud); *Davis* v. *Birr, Wilson & Co., Inc.*, 839 F.2d 1369, 1369-70 (9th Cir. 1988) (California fraud); *deHaas* v. *Empire Petroleum Co.*, 435 F.2d 1223, 1225 (10th Cir. 1970) (Colorado fraud); *Carothers* v. *Rice*, 633 F.2d 7, 15 (6th Cir. 1980) (Kentucky blue sky law), *cert. denied*, 450 U.S. 998 (1981); *In re Professional Fin. Management, Ltd.*, 703 F. Supp. 1388, 1392-93 (D. Minn. 1989) (Minnesota blue sky law); *Mid-Carolina Oil, Inc.* v. *Klippel*, 526 F. Supp. 694, 696-97 (D.S.C. 1981) (South Carolina blue sky law), *aff'd*, 673 F.2d 1313 (3d Cir.), *cert. denied*, 457 U.S. 1107 (1982); *Loveridge* v. *Dreagoux*, 678 F.2d 870, 874 (10th Cir. 1982) (Utah fraud); *Reeves* v. *Teuscher*, 881 F.2d 1495, 1500 (9th Cir. 1989) (Washington fraud); *Estate of Dearing* v. *Dearing*, 646 F. Supp. 903, 906-07 (S.D. W. Va. 1986) (West Virginia blue sky law).

[30] These States are Ohio and Texas. *See Marx* v. *Centran Corp.*, 747 F.2d 1536, 1551 (6th Cir. 1984) (Ohio fraud), *cert. denied*, 471 U.S. 1125 (1985); *Sioux, Ltd., Sec. Litig.* v. *Coopers & Lybrand*, 914 F.2d 61, 63 (5th Cir. 1990) (Texas fraud).

[31] These States are Arkansas and Massachusetts. *See, e.g., Pinney* v. *Edward D. Jones & Co., Inc.*, 718 F. Supp. 1419, 1421 (W.D. Ark. 1989) (Arkansas blue sky law); *Maggio* v. *Gerard Freezer & Ice Co.*, 824 F.2d 123, 124 & n.2 (1st Cir. 1987) (Massachusetts personal tort). *But see Robertson* v. *Deloitte, Haskins & Sells*, 732 F. Supp. 979, 985 (E.D. Ark. 1990) (applying federal one-year/three-year limitations provision); *In re Atlantic Fin. Management, Inc. Sec. Lit.*, 718 F. Supp. 1003, 1009 (D. Mass. 1988) (borrowing Massachusetts two-year blue sky law).

[32] Hawaii, Michigan, New Hampshire and South Dakota use six years. *See, e.g., Cunha* v. *Ward Foods, Inc.*, 501 F. Supp. 830, 837 (D. Haw. 1980) (Hawaii "catch-all" limitations statute); *IDS Progressive Fund, Inc.* v. *First of Michigan Corp.*, 533 F.2d 340, 344 (6th Cir. 1976) (Michigan fraud); *Seidel* v. *Public Serv. Co. of New Hampshire*, 616 F. Supp. 1342, 1358 n.24 (N.D.N.H. 1985) (New Hampshire fraud); *Rude*

In several States it simply is not clear which limitations period applies.[33] For example, the Eastern District of Tennessee uses a one-year/two-year limitations provision, while the Western District of that State employs a single three-year period. *Compare Montcastle* v. *American Health Systems, Inc.*, 702 F. Supp. 1369, 1372 (E.D. Tenn. 1988) (applying one year from discovery/two years from transaction statute of limitations from Tennessee blue sky law) *with Media General, Inc.* v. *Tanner*, 625 F. Supp. 237, 245-47 (W.D. Tenn. 1985) (applying three-year statute of limitations for common law fraud). In the Middle District of Tennessee, the limitations period seems to depend on which judge is assigned to the case. *Compare Nichols* v. *Merrill Lynch, Pierce, Fenner & Smith*, 706 F. Supp. 1309, 1320-21 (M.D. Tenn. 1989) (Higgins, J.) (applying three-year fraud statute of limitations) *with Logan* v. *Ledford*, 699 F. Supp. 141, 144 (M.D. Tenn. 1988) (Wiseman, C.J.) (applying one year from discovery/two years from transaction blue sky statute of limitations).

Federal courts in some States have applied one limitations period for a while and then borrowed a different

v. *Campbell Square, Inc.*, 411 F. Supp. 1040, 1048 (D.S.D. 1976) (South Dakota fraud).

[33] No federal court has addressed the applicable limitations period for § 10(b) claims brought in Idaho, Nebraska, Nevada, or North Dakota. In New Mexico, Rhode Island and Wyoming, cases do not resolve which limitations period is appropriate. *See Stone* v. *Fossil Oil & Gas*, 657 F. Supp. 1449, 1458 (D.N.M. 1987) (referring to New Mexico limitations periods for both state securities act and common law fraud violations, but not finding it necessary for holding to determine which period was applicable); *Holmes* v. *Bateson*, 583 F.2d 542, 559-60 (1st Cir. 1978) (mentioning both three-year limitations period for personal injuries and six-year limitation period for fraud, but declining to decide which was applicable to Rhode Island action); *Bath* v. *Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817, 818-19 (10th Cir. 1990) (reversing District Court's decision to borrow one-year/three-year limitations provision from federal securities law, remanding "for further proceedings under the most analogous state law limitations period," but not specifying which Wyoming limitations period was most analogous).

period because of changes in state law. For example, until recently courts in the Fifth Circuit applied a two-year limitations period to § 10(b) claims arising in Texas under the assumption that Texas had a two-year statute of limitations for fraud. *See, e.g., Wood* v. *Combustion Engineering, Inc.*, 643 F.2d 339, 346 (5th Cir. 1981). In March 1990, the Texas Supreme Court held that a 1979 statutory amendment had extended the limitations period for fraud to four years and that courts had been applying the incorrect limitations period for the past eleven years. *See Williams* v. *Khalaf*, No. C-8467 (Tex. Mar. 28, 1990). In response to *Williams*, the Fifth Circuit promptly reversed itself and applied a four-year limitations period to a § 10(b) claim arising in Texas. *See Sioux, Ltd., Securities Litigation* v. *Coopers & Lybrand*, 914 F.2d 61, 63 (5th Cir. 1990).

In some cases, a federal court will borrow the law of the forum; in others a federal court will apply state choice of law principles to borrow the law of another jurisdiction. *See Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990), slip op., at 6-7.

Finally, the confusion is aggravated by application of amorphous and conflicting principles of equitable tolling to determine when state limitations periods begin to run. The federal courts have "grappled at length with the interaction between state and federal tolling rules," *Short*, 908 F.2d, at 1389, and there is disagreement with respect to important facets of the federal equitable tolling doctrine.[34]

[34] In this case, the court below looked to the federal doctrine of equitable tolling to determine when the Oregon limitations period began to run. Pet. App. 12a-13a. Under the Ninth Circuit's equitable tolling rule, the limitations period "starts upon 'actual or inquiry notice that a fraudulent misrepresentation has been made,' " Pet. App. 13a (quoting *Volk* v. *D.A. Davidson Co.*, 816 F.2d 1406, 1412 (9th Cir. 1987)), and inquiry notice, which "arises when plaintiff could discover the fraud through the exercise of reasonable diligence," is tested by an " 'ob-

2. The Practice of Borrowing State Limitations Periods Has Had Pernicious Effects on § 10(b) Litigation.

The practice of applying state limitations periods to § 10(b) claims has been damaging to litigants and to the civil justice system and has undermined the effectiveness and value of §10(b) as a remedy. For example, forum shopping is inevitable and common in § 10(b) cases. *See* Respondents' Opp. to Pet. for Cert., at 4 ("There is undoubtedly forum shopping where a 10b-5 action may be brought in more than one state and the statutes of limitations differ."). Section 10(b) claims must be predicated upon conduct with a nexus to interstate commerce, and acts that typically form the basis of a complaint occur in several States. *See Ceres Partners*, slip op., at 28 ("It is hardly uncommon for a single lawsuit to encompass the claims of plaintiffs from a large number of states."); *cf. Agency Holding Corp.*, 483 U.S., at 154 (given the "multistate nature of RICO," the "use of state statutes would present the danger of forum shopping"). Indeed, the case at bar, which did not even arise out of a transaction on a national exchange, involves parties and conduct in Oregon, New York, New Jersey, Illinois, North Carolina, Pennsylvania, Texas, Delaware, Minnesota, and Connecticut.

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jective standard.' " Pet. App. 13a (citation omitted). Other courts appear to consider subjective factors in applying the "reasonable diligence" test. *See, e.g., Ohio* v. *Peterson, Lowry, Rall, Barber & Ross*, 472 F. Supp. 402, 408 (D. Colo. 1979) ("the court gives some weight to the . . . legal sophistication of the party involved"), *aff'd*, 651 F.2d 687 (10th Cir.), *cert. denied*, 454 U.S. 895 (1981). The lower federal courts also appear to disagree on the issue whether a defendant's active concealment of a fraud relieves a plaintiff of the duty of diligent investigation. *See* ABA Committee on Federal Regulations of Securities, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 655 (1986) ("ABA Report"). "The federal equitable tolling doctrine, therefore, greatly compounds the complexity of the law of limitations in implied actions for securities fraud." *Id.*

The 1934 Act's liberal venue provisions give plaintiffs wide latitude in choosing a forum.[35] A plaintiff who has unduly delayed filing a claim can almost invariably find a jurisdiction with a generous statute of limitations that will permit prosecution.

The combination of different potential limitations periods and multistate transactions has led to truly incomprehensible results. For example, in class actions, district courts have applied different limitations periods in the same case. *See, e.g., Kronfeld* v. *Advest, Inc.*, 675 F. Supp. 1449, 1457-58 & n.21 (S.D.N.Y. 1987) (applying 26 different statutes of limitations in § 10(b) class action); *In re National Student Marketing Litigation*, Fed. Sec. L. Rep (CCH) ¶ 97,926 (D.D.C. March 26, 1981) (noting the possible applicability of 34 different statutes of limitations to § 10(b) claims).

Under the current system, a lawyer sued in New Hampshire is subject to a six-year statute of limitations. *See Seidel* v. *Public Service Co. of New Hampshire*, 616 F. Supp. 1342, 1358 n.24 (D.N.H. 1985). A lawyer who performed identical functions in the same place, but who is sued in Texas, would be subject to a four-year statute of limitations. *See Longden* v. *Sunderman*, 737 F. Supp. 968, 971-72 (N.D. Tex. 1990). If state law is borrowed for § 10(b) claims, the same lawyer sued in federal court in New York by New York and New Jersey residents might be subject to *different* limitations periods for each plaintiff because New York would borrow New Jersey law for the New Jersey plaintiff but not for the plaintiff from New York. *See Ceres Partners*, slip op. at 9-10. There is no rational way to justify such disparities. Duties, rights and remedies under the national securities laws should not vary from

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[35] Section 27, 15 U.S.C. § 78aa, provides that suit may be brought to enforce the 1934 Act in "the district wherein any act or transaction constituting the violation occurred," or "in the district wherein the defendant is found or is an inhabitant or transacts business . . . ."

case to case or from plaintiff to plaintiff. The judicial resources dissipated on the resolution of complex and arcane statute of limitations issues constitute a drain on litigants and the courts alike.

The lack of cohesion among the jurisdictions necessarily frustrates private enforcement of § 10(b), distorting both the compensatory and deterrent functions of the statute. As this Court has recognized in another context:

> Plaintiffs may be denied their just remedy if they delay in filing their claims, having wrongly postulated that the courts would apply a longer statute [of limitations]. Defendants cannot calculate their contingent liabilities, not knowing with confidence when their delicts lie in repose.

Wilson v. *Garcia*, 471 U.S., at 275 (discussing limitations period for civil rights claims under 42 U.S.C. § 1983); *see also Agency Holding Corp.*, 483 U.S., at 150. To the extent that plaintiffs must speculate regarding the applicable limitations period, problems of underdeterrence are created, and the goal of investor protection is thereby undermined. At the same time, the current system's unpredictability precludes defendants from making rational judgments about their exposure to § 10(b) litigation, leading to overdeterrence and market inefficiency.

The courts and commentators have reacted to the current state of affairs "with a unanimity unmatched in any other corner of securities law." *Short*, 908 F.2d, at 1389. The practice of applying state limitations periods to § 10(b) claims has been referred to as a "nightmare," *id.*, a "tottering parapet of a ramshackle edifice," *Norris* v. *Wirtz*, 818 F.2d, at 1332, and a "judicial travesty . . . replete with evidence of sloppy scholarship, the willingness of courts to accept dicta without analysis, and the remarkable inefficiency of the federal judicial system in resolving disputed issues of federal law," Bloomenthal, *The Statute of*

Limitations and Rule 10b-5 Claims: A Study in Judicial Lassitude, 60 U. Colo. L. Rev. 235, 236 (1989).[36] In 1986, an American Bar Association special task force surveyed the state of the law and found "uncertainty," "inconsistency," "confusion" and "disarray." ABA Report, *supra* note 34, at 647, 648.

The ABA Report concluded:

> Such disarray serves no public purpose. This uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of parties litigating identical claims in different states. Neither plaintiffs nor defendants can determine their rights with any certainty.

Id., at 647 (footnotes omitted).

Although individual judges had begun to suggest that the existing practice was irrational and legally questionable,[37] the courts continued to apply state limitations pe-

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[36] *See also* Garrett, *The Ramshackle Edifice: Limitations Periods for Private Actions Under Rule 10b-5*, 28 Duq. L. Rev. 1 (1989); L. Loss, *Fundamentals of Securities Regulation*, 994-95 (1988); Block & Barton, *Statute of Limitations in Private Actions Under Section 10(b)—A Proposal for Achieving Uniformity*, 7 Sec. Reg. L.J. 374 (1980); Bromberg, *Curing Securities Violations: Rescission Offers and Other Techniques*, 1 J. Corp. L. 1, 9-10 (1975); Martin, *Statutes of Limitations and 10b-5 Actions; Which State Statute is Applicable?*, 29 Bus. Law. 443, 455 n.91 (1974); Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5*, 1972 Duke L.J. 1125; Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 Wayne L. Rev. 635 (1967).

[37] *See, e.g.*, *Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 463 (3d Cir. 1979) (Seitz, J., dissenting) (noting that commentators had urged that a uniform federal limitations period be adopted and stating that "[w]ere I writing on a clean slate, I would be inclined to adopt that approach."); *Norris*, 818 F.2d, at 1332; *Davis* v. *Birr, Wilson & Co., Inc.*, 839 F.2d 1369, 1370 (9th Cir. 1988) (Aldisert, J., concurring) (sitting by designation) (urging adoption of uniform federal limitations period).

riods to § 10(b) cases until 1988. In that year, following the guidance of this Court's decisions in *DelCostello* and *Agency Holding Corp.*, the Courts of Appeals began the process of repudiating the logic and legality of borrowing state limitations periods in § 10(b) cases. In *In Re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1550 (3d Cir.) (*en banc*), *cert. denied*, 488 U.S. 849 (1988), the Third Circuit held that § 10(b) claims should be governed by a uniform federal statute of limitations—the one-year/three-year period contained in most of the express remedy provisions of the federal securities laws. The Second and Seventh Circuits have now reached the same conclusion. *See Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990); *Short* v. *Belleville Shoe Manufacturing Co.*, 908 F.2d 1385, 1389 (7th Cir. 1990), *cert. pending* (No. 90-526).[38] As the following discussion will demonstrate, these three Courts of Appeals are correct.

C. The Federal Securities Laws Contain Explicit Remedial Provisions Far More Analogous to § 10(b) Claims Than Any State Law Alternative.

1. The One-Year/Three-Year Limitations Period Should Be Applied to § 10(b) Claims.

Section 10(b) is one of several closely related provisions that the Seventy-Third Congress included in the original securities acts with the common purpose of compelling full and truthful disclosure in securities transactions. Indeed, §§ 11 and 12 of the 1933 Act, 15 U.S.C. §§ 77k, 77*l*, and §§ 9 and 18 of the 1934 Act, 15 U.S.C. §§ 78i, 78r, were enacted by the same Congress and for the same purpose as § 10(b), and every one of these "comparable express

[38] Some federal district courts in other circuits also have applied the one-year/three-year limitations rule to § 10(b) claims. *See, e.g., Robertson* v. *Deloitte, Haskins & Sells*, 732 F. Supp. 979 (E.D. Ark. 1990).

causes of action"[39] is governed by an identical limitations period that requires commencement of a private action within one year of the discovery of the facts constituting the violation *and* within three years of the date of the violation.[40] Section 29 of the 1934 Act, amended in 1938 to permit private suits to void certain contracts, is governed by the same limitations period.[41] These sections supply a "far closer analogy"[42] to § 10(b) than any state law alternative.

There is a "substantial overlap" and "family resemblance," *DelCostello*, 462 U.S., at 170, between the express remedies of the 1933 and 1934 Acts and § 10(b). As noted earlier, §§ 11 and 12 of the 1933 Act created private remedies for false and misleading statements in connection with initial distributions of securities. Sections 9 and 18 of the 1934 Act permit private actions for similar conduct that occurs in post-issuance trading. Section 10(b) of the 1934 Act is a broad "catch-all" prohibition against all other, or new forms of "manipulative and deceptive device[s] or contrivance[s]" that was intended to give the Commission the power and flexibility to regulate new fraudulent practices not specifically identified or defined in the 1933 and 1934 Acts. *See Ernst & Ernst*, 425 U.S., at 204-05.

[39] *Blue Chip Stamps*, 421 U.S., at 736.

[40] *See* 1933 Act, § 13, 15 U.S.C. § 77m (creating one-year/three-year limitations period for private actions under §§ 11 and 12); 1934 Act, § 9(e), 15 U.S.C. § 78i(e) (precluding private actions unless "brought within one year after discovery of the facts constituting the violation and within three years after such violation"); 1934 Act, § 18(c), 15 U.S.C. § 78r(c) (precluding private actions "unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued").

[41] *See* 1934 Act, § 29(b), 15 U.S.C. § 78cc(b) (precluding actions unless "brought within one year after the discovery that [a] sale or purchase involve[d] . . . [a] violation and within three years after such violation").

[42] *Agency Holding*, 483 U.S., at 156.

The closest analog for § 10(b) is the section that immediately precedes it in the 1934 Act. Section 9, 15 U.S.C. § 78i, has been characterized as "the very heart of the act."[43] It proscribes a variety of specifically identified deceptive, manipulative or misleading practices and creates a private right of action for willful participation in any of those practices. For example, an investor may bring an action under § 9(a)(4) against certain persons who make

> any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact.

15 U.S.C. § 78i(a)(4). Rule 10b-5 uses almost identical language in creating, by inference, a right of action against someone who communicates

> any untrue statement of a material fact or . . . omit[s] to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading.

17 C.F.R. § 240.10b-5(b).

As the Second Circuit concluded in *Ceres Partners*, a suit predicated upon the conduct described in § 9 "could as easily be brought under Rule 10b-5." Slip op., at 30. In fact, although § 9 only applies to transactions involving securities registered on a national securities exchange, it

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[43] Securities and Exchange Commission, *Report on Proposals for Amendments of the Securities Act of 1933 and the Securities Exchange Act of 1934*, H.R. Comm. Print, 77th Cong. 1st Sess. 50 (1941); *see also* 78 Cong. Rec. 7865 (May 1, 1934) (statement of Rep. Wolverton) (§ 9 "recognizes and labels distinctly and unmistakably each and every such fraudulent and improper device heretofore used . . . . [I]n addition to the declaration of criminal responsibility, there is also provided civil liability in favor of any person injured by any such transaction. If anyone should desire to observe a real, genuine set of legislative teeth, he can do so by giving consideration to section [9] of this act.").

has been incorporated by reference into § 10(b) for over-the-counter transactions.[44]

This Court has refused to interpret "the catch all provision of § 10(b) . . . more broadly" than § 9, *Ernst & Ernst*, 425 U.S., at 206, holding that private parties proceeding under either section must demonstrate scienter—intent to "deceive, manipulate or defraud." *Id.*, at 193.

Section 18 of the 1934 Act is also similar to § 10(b). It creates liability for any false or misleading statement in a document filed with the Commission, 15 U.S.C. § 78r(a), and requires a showing of scienter or something closely akin to it. *See Ernst & Ernst*, 425 U.S., at 209 n.28. Conduct that violates § 18 also has been assumed to give rise to a § 10(b) claim. *See, e.g., Wilson* v. *Great American Indus., Inc.*, 855 F.2d 987, 991 (2d Cir. 1988); *Wachovia Bank & Trust Co.* v. *National Student Marketing Corp.*, 650 F.2d 342, 356-57 (D.C. Cir. 1980), *cert. denied*, 452 U.S. 954 (1981); *see also Ceres Partners*, slip op., at 30.

In 1938, Congress amended § 29 of the 1934 Act to add an express private right of action to rescind contracts that violate the statute. *See* 15 U.S.C. § 78cc(b). Section 29(b)'s private remedy was "[o]ne of the justifications advanced for implication of a cause of action under § 10(b) . . . ." *Blue Chip Stamps*, 421 U.S., at 723. In fact, the first case to recognize an implied private right of action under § 10(b) found that the claim in that case also "could be grounded upon [§] 29(b) . . . ." *Kardon* v. *National Gypsum Co.*, 69

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[44] *See, e.g., Edward J. Mawod & Co.* v. *SEC*, 591 F.2d 588, 595 (10th Cir. 1979); *SEC* v. *Resch-Cassin & Co.*, 362 F. Supp. 964, 976-78 (S.D.N.Y. 1973). *See generally* McLucas & Angotti, *Market Manipulation*, 22 Sec. & Commodities Reg. 103, 108 (1989) (discussing the substantial overlap between §§ 9 and 10(b)). Other courts also have recognized that the same conduct may be cognizable under both sections. *See Chemetron Corp.* v. *Business Funds, Inc.*, 718 F.2d 725, 727 (5th Cir. 1983); *Wolgin* v. *Magic Marker Corp.*, 82 F.R.D. 168, 179-80 (E.D. Pa. 1979).

F. Supp. 512, 514 (E.D. Pa. 1946). In another early case, the Third Circuit expressly premised its conclusion that a private right of action existed for § 10(b) violations on the "remedy . . . supplied by § 29(b) . . . . " *Slavin* v. *Germantown Fire Insurance Co.*, 174 F.2d 799, 814 (3d Cir. 1949). Section 10(b) private remedies are thus analytically and historically related to § 29(b) claims.

As the Third Circuit recognized in *Data Access*, § 10(b) "and its companion provisions [in the 1934 Act] . . . are aimed at the same objectives." 843 F.2d, at 1548. Indeed,

> [a]ll aim to compensate the same type of injury. All are designed to fill a void in the common law and to create remedies that would be uniform throughout our nation's commercial universe . . . .

Id., at 1548-49; *see also Ernst & Ernst*, 425 U.S., at 204-05. By establishing a one-year/three-year limitations period for actions charging violations of §§ 9, 18 and 29 of the 1934 Act, Congress has therefore "spoken directly to the appropriate statute of limitations for litigation of the sort" involved in § 10(b) cases. *Short*, 908 F.2d, at 1388.[45]

The express remedies of the 1933 Act also overlap with § 10(b).[46] *See Herman & MacLean*, 459 U.S., at 383-86. Indeed, the claims involved in this case—false statements to investors in original offering documents—are analogous to claims for false statements in the offer or sale of a security under § 12(2), 15 U.S.C. § 77*l*(2), as well as a cause of action under § 11, 15 U.S.C. § 77k, for false or

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[45] As discussed in the Brief of Arthur Andersen & Co., *et al.* as Amici Curiae, this manifestation of legislative intent is by itself dispositive of the question presented in this case.

[46] Although §§ 11 and 12 of the 1933 Act do not require proof of scienter, *see Ernst & Ernst*, 425 U.S., at 208, this Court has treated them as generally comparable to § 10(b). *See, e.g., Blue Chip Stamps*, 421 U.S., at 736.

misleading statements in a registration statement. *See Short*, 908 F.2d, at 1388.

In *Herman & MacLean*, 459 U.S., at 383-86, the Court reiterated that the remedial structure of the securities acts is cumulative in nature and suggested that the express and implied remedies should be construed to complement and reinforce one another. *See id.*, at 386, *and cases cited.*[47] Therefore, the same one-year/three-year limitations period that governs the express remedies in the two principal securities acts enacted by the Seventy-Third Congress should also be applied to the remedy implicit in § 10(b).

2. The Federal Policies at Stake—Investor Protection and Market Efficiency—and the Unique Practical Aspects of § 10(b) Litigation Require Application of the One-Year/Three-Year Rule.

The 1933 and 1934 Acts had two similar and overriding policy goals: creating and maintaining healthy and efficient securities markets and ensuring that investors who participated in those markets are adequately protected from fraudulent and deceptive practices. The one-year/three-year limitations period meshed comfortably with these goals. It allowed private claimants adequate time to recover damages for fraud and yet accommodated the interest of the investment community in certainty, stability and repose.

In establishing the one-year/three-year rule, Congress considered and rejected several alternative limitations periods, ranging from two to ten years. The original proposals for the 1933 Act contained no statute of

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[47] In *Herman & MacLean*, 459 U.S., at 387, the Court held, *inter alia*, that a party is not precluded from invoking § 10(b) simply because allegedly fraudulent conduct also might be subject to an express remedy under § 11.

limitations.[48] In the face of criticism,[49] the Senate adopted a bill with a five-year limitations period commencing on the date the cause of action arose.[50] The House responded by proposing a two-year/ten-year limitations provision.[51] The limitations periods of the House bill were eventually adopted for actions under §§ 11 and 12 of the 1933 Act.[52]

Early proposals for the 1934 Act contained a single limitations period of two years[53] and then a two-year/six-year limitations provision.[54] In response to criticism that the proposed 1934 Act and the newly enacted 1933 Act would deter and stifle legitimate business activity,[55] the

[48] *See* S. 875, 73d Cong., 1st Sess. (Mar. 29, 1983), *reprinted in* 3 J. Ellenberger & E. Mahar, *supra* note 4, at Item 28; H.R. 4314, 73d Cong., 1st Sess. (Mar. 29, 1933), *reprinted in* 3 J. Ellenberger & E. Mahar, *supra* note 4, at Item 22.

[49] *See Federal Securities Act: Hearing on H.R. 4314 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 1st Sess. 169 (1933) (statement of William C. Breed, representing the Investment Bankers Ass'n of Am.) (commenting that without a statute of limitations "a crook or an unprincipled lawyer can, not merely next week, but 10 years and 20 years . . . from today" bring suit), *reprinted in* 2 J. Ellenberger & E. Mahar, *supra* note 4, at Item 20.

[50] *See* S. 875, § 9, 73d Cong., 1st Sess. (Apr. 27, 1933), *reprinted in* 1 Fed. Bar Ass'n Sec. L. Comm., *Federal Securities Law Legislative History 1933-1982* 76 (1983).

[51] *See* H.R. 5480, 73d Cong., 1st Sess. (May 4, 1933), *reprinted in* 3 J. Ellenberger & E. Mahar, *supra* note 4, at Item 25.

[52] *See* Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74, *reprinted in* 1 J. Ellenberger & E. Mahar, *supra* note 4, at Item 1.

[53] *See* S. 2693, 73d Cong., 2d Sess. (Feb. 9, 1934), *reprinted in* 11 J. Ellenberger & E. Mahar, *supra* note 4, at Item 34; H.R. 7852, 73d Cong., 2d Sess. (Feb. 10, 1934), *reprinted in* 10 J. Ellenberger & E. Mahar, *supra* note 4, at Item 24.

[54] *See* S. 3420, 73d Cong., 2d Sess. (Apr. 20, 1934), *reprinted in* 11 J. Ellenberger & E. Mahar, *supra* note 4, at Item 37.

[55] *See, e.g.*, 78 Cong. Rec. 7716 (Apr. 30, 1934) (statement of Rep. Ford) ("No more controversial measure has been before the House than

Senate adopted amendments that, *inter alia*, created one-year/five-year statutes of limitations for both the 1933 Act and the proposed 1934 Act.[56] Congress ultimately reduced the limitations period to the one-year/three-year standard that now applies to §§ 9 and 18 of the 1934 Act and §§ 11 and 12 of the 1933 Act.

It is apparent from the legislative history that Congress acted quite deliberately in shortening the outside limitations period from ten years to five years, and, finally, to three years, because it was concerned that a longer limitations period would expose "honest businesses"—and even those accused of improper conduct—to intolerable and inefficient litigation contingencies. For example, a longer limitations period would have created an unhealthy disincentive for individuals to serve as corporate directors and officers.[57]

. . . the securities exchange bill of 1934."); 78 Cong. Rec. 8283 (May 8, 1934) (statement of Sen. Walcott) ("From all sections of the country have come complaints that the Securities Act of 1933 has had the effect of retarding business recovery to a considerable extent.").

[56] *See* H.R. 9323 as passed Senate with Senate Amendments, 73d Cong., 2d Sess. (1934), *reprinted in* 10 J. Ellenberger & E. Mahar, *supra* note 4, at Item 32; 78 Cong. Rec. 8668 (May 12, 1934) (statement of Sen. Fletcher in proposing amendments) (explaining that amendments were intended "to meet objections and criticisms and complaints" that the 1933 Act was "too drastic").

[57] *See, e.g.*, 78 Cong. Rec. 10185 (June 1, 1934) (statement of Sen. Byrnes) (commenting that "[t]he provisions of the Securities Act of 1933 which have caused the greatest complaint are those as to the civil liability of underwriters and of the officers and directors of corporations on account of false statements in the registration statements filed by the corporation"). Senator Byrnes noted that by shortening the limitations period from two years/ten years to one year/three years in the 1933 Act, Congress gave "greater assurance to the honest officials of a corporation." *Id.*; *see also* 78 Cong. Rec. 8198 (May 7, 1934) (statement of Sen. Byrnes) (noting that purpose of outside limitations period was to "bring to an end [the corporate director's] fear, or the fear of his estate, of a suit").

Similarly, Congress sought to protect corporate officials from stale claims by making the outside three-year limitations period absolute, that is, not subject to equitable tolling. *See Norris* v. *Wirtz*, 818 F.2d, at 1332 ("The legislative history in 1934 makes it pellucid that Congress included statutes of repose because of fear that lingering liabilities would disrupt normal business and facilitate false claims. It was understood that the three-year rule was to be absolute."); *Short*, 908 F.2d, at 1391; *Data Access*, 843 F.2d, at 1546; ABA Report, *supra* note 34, at 655. Congress was clearly aware that securities violations, particularly those involving fraud, could conceivably be hidden from injured parties for several years. Nevertheless, it rejected arguments that the commencement of the limitations period should be tolled until the plaintiff discovered the violation.[58] For actions governed by the one-year/three-

[58] One of the early proposals for the 1934 Act required that actions be brought within two years after the plaintiff discovered the securities violation but did not set an outside limit on the time for filing suit. Thus, equitable tolling was unlimited until discovery of the right of action. Thomas Corcoran, one of the drafters of this legislation, defended the decision not to include an outside limitations period against heated questioning from Senator Hamilton Kean during a Senate hearing on the legislation. *See Stock Exchange Practices: Hearings on S. Res. 84 and S. Res. 97 Before the Senate Subcomm. on Banking and Currency*, 73d Cong., 1st Sess. 6565 (1934) (Corcoran defending limitations provision, which Senator Kean called "nothing but blackmail"), *reprinted in* 6 J. Ellenberger & E. Mahar, *supra* note 4, at Item 22. Eventually, Senator Kean's position prevailed when a limitations period was added setting a maximum time for filing suit.

Later on the Senate floor, Senator Barkley pointed out the difficulties inherent in setting a limitations period for actions that involve fraud, which he noted was often difficult to discover. *See* 78 Cong. Rec. 8200 (May 7, 1934) (statement of Sen. Barkley) (arguing that Senate needed to distinguish between an injury such as a bodily tort, which is readily discovered, and an injury caused by fraud, which may take several years to discover). He contended that

> it would be manifestly unfair . . . to limit any damaged party to 1 year or 2 years or 3 years in the bringing of a suit, because it may sometimes take 4 or 5 years to discover that a fraud has been committed in a statement of facts or in the omission of a statement with reference to a share of stock or a report which may be made based upon the condition of a company.

Id. Congress definitively rejected Senator Barkley's position and adopted a three-year outside limitations period for most of the express actions under the 1934 Act.

year limitations period, Congress intended for suits to be barred at the end of the three-year period, even if the plaintiff had not discovered the violation by then. 78 Cong. Rec. 8198 (May 7, 1934) (statement of Sen. Fletcher).

Congress, therefore, considered the arguments and firmly decided that private antifraud actions should not be maintainable more than three years after the alleged violation. There are strong reasons to support this decision. Indeed, in the context of § 10(b) actions this Court has stated that

> even a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial so long as he may prevent the suit from being resolved against him by dismissal or summary judgment. *The very pendency of the lawsuit may frustrate or delay normal business activity of the defendant which is totally unrelated to the lawsuit.*

Blue Chip Stamps, 421 U.S., at 740 (emphasis added);[59] *see also Ernst & Ernst*, 425 U.S., at 214 n.33. In fact,

[59] *In Blue Chip Stamps*, the Court expressly analogized § 10(b) to § 11 of the 1933 Act. It is most significant that the *Blue Chip Stamps* Court went on to emphasize that "Congress itself recognized the potential for nuisance or 'strike' suits in this type of litigation," 421 U.S., at 740, and in 1934 amended § 11 of the 1933 Act to include a provision

"[t]here has been widespread recognition that litigation under Rule 10b-5 presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general." *Blue Chip Stamps*, 421 U.S., at 739.

These "practicalities of litigation" blend with the federal policies that uniformly underlie § 10(b) and the other private antifraud actions to make the finite one-year/three-year period a "significantly more appropriate" limitations period for § 10(b) claims than any conceivable state law alternative.[60] *Cf. Reves* v. *Ernst & Young*, 110 S. Ct. 945, 954 (1990) ("We are unpersuaded that Congress intended the Securities Acts to apply differently to the same transactions depending on the accident of which State's law happens to apply.").

3. The Two Limited Exceptions to the One-Year/ Three-Year Limitations Periods in the 1933 and 1934 Acts Are Not Appropriate for Application to § 10(b) Cases.

There are only two express private rights of action in the 1933 and 1934 Acts not governed by the one-year/ three-year limitations period: § 16(b) of the 1934 Act, 15 U.S.C. § 78p(b), which contains a two-year statute of limitations, and § 20A of the 1934 Act (added by the Insider

allowing courts to require plaintiffs to post an undertaking against costs to act as a deterrent against frivolous suits. The Court concluded that "that fact alone justifies our consideration of such potential in determining the limits of the class of plaintiffs who may sue in an action wholly implied from the language of the 1934 Act." *Id.*, at 741. The Court could also have noted that at the same time in 1934 that the provision regarding undertakings for costs was added, the statute of limitations for private actions under § 11 of the 1933 Act was shortened to the present one-year/three-year standard.

[60] The Commission itself is not limited by the one-year/three-year limitation periods. It has enforcement authority to pursue actions under §§ 11 and 12 of the 1933 Act and §§ 9, 10, 18, and 29 of the 1934 Act at any time, even if more than three years have passed since the violation.

Trading and Securities Fraud Enforcement Act of 1988 ("ITSFEA")), 15 U.S.C. § 78t-1, which has a five-year limitations period. For both sections, Congress carved out a narrow class of cases to receive special treatment based upon the unique substantive nature of the cause of action involved.

a. Section 16(b) of the 1934 Act.

Unlike § 10(b), § 16(b) "is not a disclosure section." *Ceres Partners*, slip op., at 32. Section 16(b) permits a shareholder to sue on behalf of a corporation to compel disgorgement of "short-swing" profits of certain corporate insiders[61] who engage in a purchase and sale within a six-month period. It is a prophylactic statute that imposes virtually absolute liability and requires reimbursement of profits even "without proof of actual abuse of insider information, and without proof of intent to profit on the basis of such information." *Kern County Land Co.* v. *Occidental Petroleum Corp.*, 411 U.S. 582, 595 (1973). Because § 16(b) is so different from § 10(b), it requires little elaboration to explain that § 16 is not a proper § 10(b) analog for statute of limitations purposes. Both *Ceres Partners*, slip op., at 32-33, and *Data Access*, 843 F.2d, at 1546, expressly concluded that these substantive differences between § 16(b) claims and claims under §§ 9, 10 and 18 made the two-year limitations period an inappropriate choice for § 10(b) claims.

b. Section 20A of the 1934 Act.

Section 20A of the ITSFEA is also expressly and unambiguously directed toward a narrow species of cases. It provides a remedy against an individual who violates other provisions of the securities acts "by purchasing or selling a security while in possession of material nonpublic infor-

[61] Section 16 applies to directors, officers and any person who is the "beneficial owner" of more than 10% of any class of an equity security. 15 U.S.C. § 78p(a).

mation" in favor of a person who contemporaneously with such transaction also purchased or sold the same class of securities. *See* 15 U.S.C. § 78t-1(a).[62] Section 20A was "specifically intended to overturn court cases which have precluded recovery for plaintiffs where the defendant's violation is premised upon the misappropriation theory." H. R. Rep. No. 910, 100th Cong., 2d Sess., at 26, *reprinted in* 1988 U.S.C.C.A.N., at 6063.[63] Therefore, § 20A permits a remedy for insider trading for violations of other provisions of the 1933 and 1934 Acts in circumstances in which a remedy was not otherwise available under the securities laws.

Section 20A is materially different from § 10(b) in many respects. It is a narrowly tailored private remedy to address a specific violation, whereas § 10(b) is a broad, ov-

[62] Section 20A was only one small part of the ITSFEA legislation. The key feature of the ITSFEA was § 21A, which authorized the Commission to seek treble civil penalties from "controlling persons" in certain insider trading cases. *See* H.R. Rep. No. 910, 100th Cong. 2d, Sess. 15, *reprinted in* 1988 U.S. Code Cong. & Admin. News 6043, 6052 ("U.S.C.C.A.N."). In addition, the ITSFEA created a "bounty" program that allows the Commission to reward informants; mandated that broker-dealers and investment advisers "establish, maintain and enforce written policies 'reasonably designed' to prevent misuse of material, nonpublic information by the firm or any of its employees or associated persons", and increased the maximum term of imprisonment and fines for federal securities law violators. *See* H.R. Rep. No. 910, at 7, *reprinted in* 1988 U.S.C.C.A.N., at 6044.

[63] Such cases relied upon the rationale of *Chiarella* v. *United States*, 445 U.S. 222 (1980), in which the Court held that liability for failure to disclose material, nonpublic information depended upon the existence of a "relationship of trust and confidence" between the parties to a transaction. *Id.*, at 228. Thus, for example, in *Moss* v. *Morgan Stanley, Inc.*, 719 F.2d 5 (2d Cir. 1983), *cert. denied*, 465 U.S. 1025 (1984), the Second Circuit held that while misappropriation might provide the basis for a *criminal* prosecution for violation of § 10(b), such conduct did not in and of itself give rise to a private suit for damages absent proof that the defendant owed a fiduciary duty to the plaintiff. *Id.*, at 13-15.

erarching antifraud measure. Section 20A establishes a restitutionary, rather than compensatory remedy, expressly limiting recovery to "profit gained or loss avoided." 15 U.S.C. § 78t-1(b)(1). And it permits a defendant to offset liability for private damages by amounts disgorged in actions brought by the Commission. 15 U.S.C. § 78t-1(b)(2).

When Congress enacted a five-year limitations period for private actions under § 20A, it did not have in mind the panoply of fraudulent and deceptive practices that can form the predicate for a private suit for damages under § 10(b). In fact, Congress squarely addressed this point by stating § 20A was not to be construed to "limit or condition . . . the availability of *any action implied from a provision of this title*." 15 U.S.C. § 78t-1(d). Thus, Congress made it as plain as it could that § 20A, which has prospective effect only, *see* 15 U.S.C. § 78*o* (note), was not intended to modify or affect implied private actions, of which § 10(b) is clearly the most prominent.

Section 20A also explicitly limits application of its five-year statute of limitations to actions "brought under this section." 15 U.S.C. § 78t-1(b)(4). To apply it to § 10(b) actions not brought under § 20A "would let the tail wag the dog." *Short*, 908 F.2d., at 1392. In fact, § 20A is so constrained in its language and limited in its application that to apply its limitations period to one of "the most litigated provisions in the federal securities laws" (*SEC* v. *National Securities, Inc.*, 393 U.S., at 465) would be to let a minnow give birth to a whale.

There is nothing in the legislative history that suggests that the five-year statute of limitations for § 20A claims was intended to apply to § 10(b) implied rights of action. The antecedent Insider Trading Sanctions Act of 1984 ("ITSA"), Pub. L. No. 98-376, § 2, § 21(d)(2)(D), 98 Stat. 1264, 1265, authorized the Commission to seek treble damage penalties from inside traders. Because of the penal, nonremedial nature of the civil penalty actions under the

ITSA, Congress imposed the same limitations period for those actions that it applied to criminal cases brought under the 1934 Act, which are governed by the "catch-all" five-year statute of limitations for federal criminal prosecutions generally, *see* 18 U.S.C. § 3282.[54]

In the 1988 ITSFEA legislation, Congress extended the treble damage penalties for insider trading to certain "controlling persons" of brokerage and securities firms who fail to take adequate steps to prevent insider trading and included a five-year limitations period that was expressly incorporated from the ITSA.[55] Although the legislative history is silent with respect to § 20A's five-year statute of limitations, it appears that it, too, was modeled on the ITSA in order to ensure uniformity and consistency in the parallel enforcement scheme devised by Congress for this very narrow class of insider trading violations.

The five-year limitations period of § 20A thus appears to have its genesis in the criminal law. It therefore "does not reflect any congressional balancing of the competing equities," *Agency Holding*, 483 U.S., at 156 (rejecting application of five-year limitations period for criminal RICO actions to civil RICO claims), that are unique to civil actions for damages under § 10(b).[56]

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[54] *See generally* H.R. Rep. No. 355, 98th Cong., 2d Sess. 30 (reprinting letter from Commission Chairman John Shad to Congressman Timothy Wirth) (noting that five-year limitations period "would conform to the criminal statute of limitations for Exchange Act violations"), *reprinted* in 1984 U.S.C.C.A.N., at 2303.

[55] The House Report accompanying the ITSFEA comments that the limitations clause for § 21A suits "imposes the same statute of limitations as included in present law in Section 21(d)(2)(D) of the Exchange Act [ITSA]." H.R. Rep. No. 910, at 37, *reprinted* in 1988 U.S.C.C.A.N., at 6074.

[56] Deception by silence inheres in insider trading violations, which often involve complex conspiracies between market professionals who operate through impersonal transactions on the open market. *See* H.R. Rep. No. 910, at 15-16, 22-23, *reprinted in* 1988 U.S.C.C.A.N., at 6052-53, 6059-60 (discussing special difficulties of detecting insider trading). Thus, individuals generally will not know the identity of the persons who have defrauded them through inside trading without the benefit of a government investigation, which may take years to complete. A longer limitations period is therefore apt for § 20A violations for reasons that have no application to the more common allegations of fraud presented in this, a typical § 10(b) case, where respondents were apprised of petitioner's identity and role in the transaction even before they made their initial investment.

The paucity of legislative history concerning the limitations provision contained in § 20A confirms that Congress gave the subject little consideration and certainly did not intend for that provision to serve as a standard for the limitations periods of other private rights of action in the federal securities laws. In contrast, as demonstrated above, the extensive legislative history addressing the one-year/three-year limitations provisions of the other express private rights of action reveals an affirmative and considered congressional judgment to reject a five-year limitations period for private civil fraud actions under the federal securities laws.[57]

All of the courts that have considered the issue have rejected § 20A's five-year statute of limitations as an appropriate standard for § 10(b) and have chosen the one-year/three-year period instead. In *Ceres Partners*, the Second Circuit observed that, "plainly Congress felt that unique measures were necessary to curb insider trading, and we are not persuaded that the five-year limitations period specified for that type of action, which has not been designated for any other type of securities claim, was one that Congress meant to apply generally." Slip op., at 35. In *Short*, the court held that "Congress did not say that § 20A applies to all cases under Rule 10b-5 . . . [I]t limited

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[57] As discussed *supra*, at page 39, the Senate proposal for the 1934 Act included a one-year/five-year limitations period, which was rejected in favor of the one-year/three-year statute of limitations.

the scope of § 20A's statute of limitations to a particular and atypical kind of violation."). 908 F.2d, at 1392.[68]

It would be particularly inappropriate and incongruous to choose a limitations period that exceeds the one-year/three-year period contained in the "principal express nonderivative private civil remedies, created by Congress contemporaneously with the passage of § 10(b) . . . ." *Blue Chip Stamps*, 421 U.S., at 735-36. In fact, application of a five-year limitations period for actions under § 10(b) would effectively nullify the one-year/three-year statute of limitations for the expressly created remedies under the 1933 and 1934 Acts. Plaintiffs would simply plead and prosecute those actions under § 10(b). Thus, selection of a judicially borrowed five-year period would have the effect of overriding an express congressional judgment as to the limitations period for these express remedies. *See Ernst & Ernst*, 425 U.S., at 210 (permitting § 10(b) claims to be premised on negligent rather than intentional wrongdoing would 'nullify the effectiveness of the carefully drawn procedural restrictions on these express actions"); *Blue Chip Stamps*, 421 U.S., at 736 n.8; ABA Report, *supra* note 34, at 647 n.19. On the other hand, selection of the one-year/three-year period would not only preserve the congressional determination for the express antifraud remedies in the 1933 and 1934 Acts, but would also leave intact the five-year limitation window for actions under the ITSFEA. As this Court squarely held in *Blue Chip Stamps*, "[i]t would indeed be anomalous to impute to Congress an intention to expand the plaintiff class for a ju-

[68] The District Court in *Ceres Partners* also found that § 20A was not a "rational alternative possible analogy" to the one-year/three-year period. 714 F. Supp. 679, 686 (S.D.N.Y. 1989) (Pollack, J.). In *Elysian Federal Savings Bank* v. *First Interregional Equity Corp.*, 713 F. Supp. 737, 743 (D.N.J. 1989), the District Court rejected the argument that the one-year/three-year rule adopted in *Data Access* prior to the enactment of § 20A "should be deemed to be modified" by § 20A's incorporation of a five-year limitations period.

dicially *implied* cause of action beyond the bounds it delineated for *comparable express* causes of action." 421 U.S., at 736. (emphasis added).

CONCLUSION

Neither the state legislatures nor Congress had any intention that private rights of action under § 10(b) of the Securities Exchange Act of 1934 should be governed by state-created statutes of limitations. Section 10(b) is a federal provision, part of a comprehensive interrelated federal regulatory scheme, intended to be enforced uniformly in federal courts in connection with multistate transactions. It is difficult to imagine a measure less amenable to the *ad hoc* application of a parade of conflicting state limitations periods. Practice has demonstrated that this approach has produced no tangible benefits, only a legacy of confusion and expense to litigants and the federal courts and dislocations to the efficient operation of the federal securities laws.

A uniform federal limitations period for § 10(b) actions under the 1934 Act is available in § 9 of the 1934 Act. And it is the same limitations period explicitly applied by Congress to every other comparable antifraud remedy that it created at the same time as § 10(b). It is the only appropriate vehicle for interstitial lawmaking that will not only advance the federal policies and the practicalities of § 10(b) litigation but also effectuate the intentions of Congress.

December 5, 1990

Respectfully submitted,

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APPENDIX

APPENDIX

Section 11(a), (b) of the Securities Act of 1933; 15 U.S.C. § 77k:

§ 77k. Civil liabilities on account of false registration statement

(a) Persons possessing cause of action; persons liable

In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director of (or person performing similar functions) or partner in the issuer at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and not knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.

(b) Persons exempt from liability upon proof of issues

Notwithstanding the provisions of subsection (a) no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof—

(1) that before the effective date of the part of the registration statement with respect to which his liability is asserted (A) he had resigned from or had taken such steps as are permitted by law to resign from, or ceased or refused to act in, every office, capacity, or relationship in which he was described in the registration statement as acting or agreeing to act, and (B) he had advised the Commission and the issuer in writing that he had taken such action and that he would not be responsible for such part of the registration statement; or

(2) that if such part of the registration statement became effective without his knowledge, upon becoming aware of such fact he forthwith acted and advised the Commission, in accordance with paragraph (1) of this subsection, and, in addition, gave reasonable public notice that such part of the registration statement had become effective without his knowledge; or

(3) that (A) as regards any part of the registration statement not purporting to be made on the authority of

an expert, and not purporting to be a copy of or extract from a report or valuation of an expert, and not purporting to be made on the authority of a public official document or statement, he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading; and (B) as regards any part of the registration statement purporting to be made upon his authority as an expert or purporting to be a copy of or extract from a report or valuation of himself as an expert, (i) he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or (ii) such part of the registration statement did not fairly represent his statement as an expert or was not a fair copy of or extract from his report or valuation as an expert; and (C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement of the expert or was not a fair copy of or extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or

purporting to be a copy of or extract from a public official document, he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue, or that there was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement made by the official person or was not a fair copy of or extract from the public official document.

• • •

Section 12 of the Securities Act of 1933, 15 U.S.C. § 77l:

§ 77l. Civil liabilities arising in connection with prospectuses and communications

Any person who—

(1) offers or sells a security in violation of section 77e of this title, or

(2) offers or sells a security (whether or not exempted by the provisions of section 77c of this title, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission, shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount

of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

Section 13 of the Securities Act of 1933, 15 U.S.C. § 77m:

§ 77m. Limitations of actions

No action shall be maintained to enforce any liability created under section 77k or 77*l*(2) of this title unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 77*l*(1) of this title, unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 77k or section 77*l*(1) of this title more than three years after the security was bona fide offered to the public, or under section 77*l*(2) of this title more than three years after the sale.

Section 9(a), (b), (c), (e) of the Securities Exchange Act of 1934, 15 U.S.C. § 78i(a), (b), (c), (e):

§ 78i. Manipulation of security prices

(a) Transactions relating to purchase or sale of security

It shall be unlawful for any person, directly or directly, by the use of the mails or any means or instrumentality of interstate commerce, or of any facility of any national securities exchange, or for any member of a national securities exchange—

(1) For the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or a false or misleading appearance with respect to the market for any such security, (A) to effect any transaction in such security which involves no change in the beneficial ownership thereof, or (B) to enter an order or orders for the purchase of such

security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties, or (C) to enter any order or orders for the sale of any such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the purchase of such security, has been or will be entered by or for the same or different parties.

(2) To effect, alone or with one or more other persons, a series of transactions in any security registered on a national securities exchange creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

(3) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination in the ordinary course of business of information to the effect that the price of any such security will or is likely to rise or fall because of market operations of any one or more persons conducted for the purpose of raising or depressing the prices of such security.

(4) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to make, regarding any security registered on a national securities exchange, for the purpose of inducing the purchase or sale of such security, any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact, and which he knew or had reasonable ground to believe was so false or misleading.

(5) For a consideration, received directly or indirectly from a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination of information to the effect that the price of any such security will or is likely to rise or fall because of the market operations of any one or more persons conducted for the purpose of raising or depressing the price of such security.

(6) To effect either alone or with one or more other persons any series of transactions for the purchase and/or sale of any security registered on a national securities exchange for the purpose of pegging, fixing, or stabilizing the price of such security in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) Transactions relating to puts, calls, straddles or options

It shall be unlawful for any person to effect, by use of any facility of a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors—

(1) any transaction in connection with any security whereby any party to such transaction acquires any put, call, straddle, or other option or privilege of buying the security from or selling the security to another without being bound to do so; or

(2) any transaction in connection with any security with relation to which he has, directly or directly, any interest in any such put, call, straddle, option, or privilege; or

(3) any transaction in any security for the account of any person who he has reason to believe has, and who actually has, directly or indirectly, any interest in any such put, call, straddle, option, or privilege with relation to such security.

(c) Endorsement or guarantee of puts, calls, straddles, or options

It shall be unlawful for any member of a national securities exchange directly or indirectly to endorse or guarantee the performance of any put, call, straddle, option, or privilege in relation to any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

* * *

(e) Persons liable; suits at law or in equity

Any person who willfully participates in any act or transaction in violation of subsections (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity of any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant. Every person who becomes liable to make any payment under this subsection may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment. No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j:

§ 78j. Manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Section 16(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78p(b):

§ 78p. Directors, officers and principal stockholders

(b) Profits from purchase and sale of security within six months

For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by

the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

Section 18(a), (c) of the Securities Exchange Act of 1934, 15 U.S.C. § 78r(a), (c):

§ 78r. Liability for misleading statements

(a) Persons liable; persons entitled to recover; defense of good faith; suit at law or in equity; costs, etc.

Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this chapter or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 78*o* of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such

reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

* * *

(c) Period of limitations

No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued.

Section 20A of the Securities Exchange Act of 1934, 15 U.S.C. § 78t-1:

§ 78t-1. Liability to contemporaneous traders for insider trading

(a) Private rights of action based on contemporaneous trading

Any person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

(b) Limitations on liability

(1) Contemporaneous trading actions limited to profit gained or loss avoided

The total amount of damages imposed under subsection (a) of this section shall not exceed the profit gained or loss avoided in the transaction or transactions that are the subject of the violation.

(2) Offsetting disgorgements against liability

The total amount of damages imposed against any person under subsection (a) of this section shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 78u(d) of this title relating to the same transaction or transactions.

(3) Controlling person liability

No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under this section shall be subject to section 78t(a) of this title.

(4) Statute of limitations

No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

(c) Joint and several liability for communicating

Any person who violates any provision of this chapter or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) of this section with, and to the same extent as, any person or persons liable under subsection (a) of this section to whom the communication was directed.

(d) Authority not to restrict other express or implied rights of action

Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this chapter or the availability of any cause of action implied from a provision of this chapter.

(e) Provisions not to affect public prosecutions

This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this chapter, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties.

Section 29(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78cc(b):

§ 78cc. Validity of contracts

(b) Contract provisions in violation of chapter

Every contract made in violation of any provision of this chapter or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made, the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this chapter or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have accrued any right thereunder with actual knowledge of the facts by reason of which the making of performance of such contract was in violation of any such provision, rule, or regulation: *Provided*, (A) That no contract shall be void by reason of this subsection because of any violation of

any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 78*o* of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 78*o* of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

Securities and Exchange Commission Rule 10b-5, 17 C.F.R. § 240.10b-5:

§ 240.10b-5. Employment of manipulative and deceptive devices

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,

(a) To employ any device, scheme, or artifice to defraud,

(b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(c) To engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person, in connection with the purchase or sale of any security.

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No. 90-333

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,
PETITIONER

v.

JOHN GILBERTSON, ET AL.,
RESPONDENTS

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF FOR RESPONDENTS COMDISCO, INC. AND KENNETH N. PONTIKES IN SUPPORT OF PETITIONER

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QUESTIONS PRESENTED

1. Whether the implied private cause of action under Section 10(b) of the Securities Exchange Act of 1934 and SEC Rule 10b-5 is subject to a uniform federal statute of limitations or to divergent limitations periods borrowed from the law of the forum state.

2. If a federal statute of limitations is applicable to 10(b) actions, whether the appropriate statute is the one-year/three-year provision in the Securities Act of 1933 and the Securities Exchange Act of 1934 or the five-year provision in the Insider Trading and Securities Fraud Enforcement Act of 1988.

RULE 29.1 STATEMENT

Comdisco, Inc. and Kenneth N. Pontikes were defendants-appellees below and, pursuant to Sup. Ct. R. 12.4, are respondents in support of petitioner in this Court. Comdisco, Inc. has no parent company. Its non-wholly-owned subsidiaries are: Comdisco Investment Group, Inc.; Comdisco Belgium S.A.; Comdisco France S.A.; Comdisco Italia, S.P.A.; Comdisco Japan, Inc.; Comdisco Portugal Computadores LDA; Comdisco, S.A.; Comdisco Financial Services VmbH; Comdisco Australia PTY Ltd.; Comdisco Espana, S.A.; Comdisco Switzerland, S.A.; Comdisco United Kingdom Limited; and Computer Discount Corporation S.A.-Madrid.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-333

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,
PETITIONER

v.

JOHN GILBERTSON, ET AL.,
RESPONDENTS

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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BRIEF FOR RESPONDENTS COMDISCO, INC. AND KENNETH N. PONTIKES IN SUPPORT OF PETITIONER

OPINIONS BELOW

The opinion of the court of appeals (Pet. App. 8a-18a) is unreported. The opinion of the district court (*id.* at 22a-43a) is unreported.

JURISDICTION

The judgment of the court of appeals was entered on February 5, 1990. A timely petition for rehearing was denied on May 16, 1990. The petition for a writ of certiorari was filed on August 10, 1990, and was granted on October 9, 1990. The jurisdiction of this Court rests on 28 U.S.C. § 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

The appendix to this brief contains the relevant provisions of the Securities Act of 1933, the Securities Exchange Act of 1934, the Insider Trading Sanctions Act of 1984, the Insider Trading and Securities Fraud Enforcement Act of 1988, and SEC Rule 10b-5.

STATEMENT

1. The facts relevant to the statute of limitations question are uncontroverted and may be briefly stated. Plaintiffs were investors in various limited partnerships formed for the purpose of purchasing and leasing computer equipment and software. Plaintiffs, "seeking tax shelters," made their investments between 1979 and 1981. Pet. App. 28a. As the district court stated (*ibid.*):

> Tax problems arose, but plaintiffs did not then attempt to investigate their claims or file this action. When the tax shelters collapsed, plaintiffs paid no heed to their investments but instead sought to resolve their tax problems.

Despite receiving continuing reports on the economic problems of the partnerships (*id.* at 31a-32a), plaintiffs did not commence this litigation until after they had reached a settlement with the Internal Revenue Service concerning the disallowance of their tax benefits. *Ibid.*

In their complaints, plaintiffs alleged that they were induced to make their 1979-1981 investments by defendants' misrepresentations in connection with the offering and sale of the limited partnership interests. Pet. App. 31a, 32a-33a. On that basis, they asserted, *inter alia*, an implied cause of action under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b). Plaintiffs first filed

this litigation in November 1986—more than five years after the last of their investments.[1]

2. Insofar as relevant here, the district court granted defendants' motion for summary judgment on statute of limitations grounds. Pet. App. 22a-43a. Following circuit precedent, the court held that Oregon's two-year statute of limitations for fraud applied to the 10(b) count. *Id.* at 35a. Because plaintiffs were on inquiry notice as early as October 1982 and failed to exercise due diligence to discover the alleged fraud, and because defendants had not fraudulently concealed the alleged violations, the court dismissed plaintiffs' 10(b) claim as barred by the two-year limitations period. *Id.* at 35a-43a.

3. The court of appeals reversed the dismissal of plaintiffs' 10(b) claim. Pet. App. 8a-18a. Like the district court, the court of appeals applied Oregon's fraud statute of limitations (*id.* at 12a). The court of appeals held, however, that plaintiffs had presented disputed issues of material fact on the questions of inquiry notice and fraudulent concealment, thereby rendering summary judgment inappropriate. *Id.* at 15a-17a.

INTRODUCTION AND SUMMARY OF ARGUMENT

1. The first issue in this case is whether the implied private cause of action under Section 10(b) of the Securities Exchange Act of 1934 is subject to (1) a uniform statute of limitations drawn from a limitations period provided in the federal securities laws for express statutory

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[1] As defendants Comdisco, Inc. and Kenneth N. Pontikes explained in their memorandum in support of summary judgment (at 27-31), plaintiffs' deliberate delay in bringing suit resulted in substantial prejudice to the defense, including witnesses' loss of memory on key issues, the absence of critical documents, and the death or disappearance of essential witnesses.

causes of action, or (2) divergent state limitations periods borrowed from the law of the forum where the particular suit is filed.[2] Our position, and that of the United States,[3] is that a uniform federal limitations period is appropriate.

This conclusion follows from two central and essentially indisputable propositions. First, with a consensus rare in the law, courts and commentators have agreed that borrowing state limitations periods in federal securities litigation is inherently impractical and undesirable. Borrowing state law has led to uncertainty and unpredictability for parties and judges, greater expense and delay in litigation, and inconsistencies and forum shopping under a statute with liberal venue provisions.

Second, in *every* instance in which Congress has enacted an express private cause of action in the securities laws, it concomitantly has provided an express federal limitations period. These limitations have been carefully designed to guard against vexatious litigation, to promote certainty for plaintiffs and defendants alike, and to ensure national uniformity. Congress plainly would have followed the same course, in furtherance of the same policies, if it had included an explicit 10(b) cause of action in the statute; there is absolutely no basis for the courts to depart from this congressional scheme in formulating the implied 10(b) cause of action. Accordingly, as judges and scholars have long advocated, the most appropriate statute of limitations

[2] SEC injunctive suits to enforce the securities laws are not subject to a statute of limitations. See 5C A. Jacobs, LITIGATION AND PRACTICE UNDER RULE 10b-5, at 10-5 & n.7 (2d ed. 1990); cf. *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 751 n.14 (1975). Such actions are not at issue in this case.

[3] The Solicitor General took this position in response to the Court's invitation to express the views of the United States in *Lebman* v. *Aktiebolaget Electrolux*, cert. denied, 109 S. Ct. 3214 (1989) (No. 88-1114). The SEC also adopted the same position in *Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990).

for 10(b) actions is found in the express federal limitations provisions in the securities laws, not in the welter of limitations periods provided by the 50 states for common law fraud, "blue sky law" violations, or other causes of action thought to be "analogous" to 10(b) claims.

2. The only remaining question is which express limitations period in the federal securities laws should be applied to 10(b) actions. It is here that we and the SEC part company. In our view, the appropriate statute of limitations for such implied actions is the statutory one-year/three-year provision applicable to the express private causes of action under the Securities Act of 1933 and the Securities Exchange Act of 1934.[4] This limitations provision reflects Congress's contemporaneous determination of the proper time period for commencing private securities suits and, because of the similarities between Section 10(b) and the express liability sections of the 1933 and 1934 Acts, best effectuates the congressional resolution of the competing policies of repose and private enforcement.

By contrast, the SEC relies on the five-year statute of limitations incorporated in the 1988 insider trading statute. That limitations period should be rejected because (a) it did not appear in the federal securities laws until some 50 years after enactment of the 1934 Act; (b) Congress specifically rejected a five-year period as too long for the express causes of action in the 1933 and 1934 Acts; (c) in enacting the 1988 statute, Congress narrowly limited the five-year limitations provision to the special situation of insider trading and deliberately did not extend it to 10(b) actions generally; and (d) the courts have noted (contrary to the premise of the government's position in *Leb-*

[4] The one-year/three-year limitation provides that suit must be brought within one year after plaintiff's discovery of the alleged violation and in no event more than three years after such violation occurred. See pages 33-34, *infra* (legislative history of provisions).

man and *Ceres Partners*) that the five-year period appears to be a statute of limitations and not, like all of the express time provisions in the 1933 and 1934 Acts, a statute of repose.[5]

In these circumstances, the SEC's submission represents a form of legislative revisionism that is irreconcilable with the history and policies of the statutes Congress enacted. The one-year/three-year provision in the 1933 and 1934 Acts, not the five-year provision created half a century later in the unique context of insider trading violations, thus supplies the appropriate limitations period for implied 10(b) actions. There can be no doubt that this is the period Congress would have chosen if it had enacted an express 10(b) action in 1934; neither the judicial implication of the right of action nor the subsequent insider trading legislation justifies a different limitations period.

ARGUMENT

THE IMPLIED PRIVATE 10(b) CAUSE OF ACTION IS SUBJECT TO A UNIFORM ONE-YEAR/THREE-YEAR FEDERAL LIMITATIONS PERIOD

The decisions of this Court consistently have recognized the critical importance of statutes of limitations to a fair and sound litigation system. The Court has "emphasized" that statutes of limitations "are not simply technicalities" but serve "importan[t] * * * policies" and "have long been respected as fundamental to a well-ordered judicial system." *Board of Regents* v. *Tomanio*, 446 U.S. 478, 487 (1980). "[S]trong policies of repose" prevent dilatory litigation that could "impair the accuracy of the fact-finding

[5] The term "statute of repose" is commonly used to refer to a limitations period that provides an absolute maximum time limit that is not subject to equitable tolling or equitable estoppel. A "statute of limitations," by contrast, is a limitations period that may be extended on such equitable grounds.

process" and "upset settled expectations that a substantive claim will be barred without respect to whether it is meritorious." *Ibid.* Thus, the "customary purpose" of statutes of limitations is

> "to promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared. The theory is that even if one has a just claim it is unjust not to put the adversary on notice to defend within the period of limitation and that the right to be free of stale claims in time comes to prevail over the right to prosecute them."

Bowen v. *City of New York*, 476 U.S. 467, 481 & n.13 (1986) (citations omitted).

Despite the evident importance of statutes of limitations, Congress does not always specify the applicable limitations period for a federal cause of action. When it does not, the Court, recognizing the "importance of policies of repose in the federal * * * system," has "borrowed" the most analogous statute of limitations to bar untimely suits. *Tomanio*, 446 U.S. at 488. To hold otherwise and thereby allow actions to "be brought at any distance of time * * * would," as Chief Justice Marshall explained, "be utterly repugnant to the genius of our laws." *Adams* v. *Woods*, 6 U.S. (2 Cranch) 336, 342 (1805), quoted in *Wilson* v. *Garcia*, 471 U.S. 261, 271 (1985).

In many cases of congressional silence, this Court has turned to state rather than federal law to find the controlling limitations period. Recent decisions make clear, however, that no rule of law mandates that result and that the Court is free to borrow the appropriate statute of limitations from either federal or state law. See *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987); *DelCostello* v. *International Bhd. of Teamsters*, 462 U.S. 151 (1983); see also *Wilson*, 471 U.S. at 270 &

nn.20, 21. Thus, "a clear majority of the Court [has] rejected * * * [the] single path * * * that federal courts always should apply the state statute of limitations most analogous to each individual case whenever a federal statute is silent on the proper limitations period." *Agency Holding*, 483 U.S. at 146. In particular, neither the Rules of Decision Act (28 U.S.C. § 1652)[6] nor the presumed intention of Congress in failing to prescribe an explicit limitations period (especially for a judicially implied rather than a legislatively created cause of action)[7] requires that a state statute of limitations be borrowed.

A state limitations period often will prove to be appropriate, particularly when the dispute is localized in nature. See, *e.g.*, *Reed* v. *United Transp. Union*, 488 U.S. 319 (1989); *Owens* v. *Okure*, 488 U.S. 235 (1989). But in other cases, the most logical limitations period is one borrowed from federal law. The decision whether to choose state or federal law in any given case depends upon a careful analysis of the particular statutory scheme involved, including the language and structure of the act, its legislative history, and its purposes and practical implementation. Under that analysis, a federal rather than a state statute of limitations should be borrowed for 10(b) actions.

I. A UNIFORM LIMITATIONS PERIOD DRAWN FROM THE FEDERAL SECURITIES LAWS IS APPLICABLE TO IMPLIED 10(b) ACTIONS

As the Ninth Circuit did in this case, courts traditionally have borrowed state limitations periods for implied 10(b) actions. This Court has noted that practice but has never

[6] See *Agency Holding*, 483 U.S. at 147; *DelCostello*, 462 U.S. at 159 n.13.

[7] See *Agency Holding*, 483 U.S. at 148; *Wilson*, 471 U.S. at 270 n.20, quoting *Auto Workers* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 709 (1966) (White, J., dissenting); *DelCostello*, 462 U.S. at 159-160 n.13.

been required to pass upon its validity. See *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 384 n.18 (1983); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 210 n.29 (1976).[8]

More recently, based on the intervening decisions of this Court in *Agency Holding*, *Wilson*, and *DelCostello*, three courts of appeals have ruled that the appropriate limitations period in 10(b) suits is to be taken from the federal securities laws rather than from state law. See *Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990); *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990) (Easterbrook, J.), petition for cert. pending, 59 U.S.L.W. 3354 (filed Sept. 26, 1990) (No. 90-526); *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.) (en banc), cert. denied, 488 U.S. 849 (1988); see also *Davis* v. *Birr, Wilson & Co.*, 839 F.2d 1369, 1370-1376 (9th Cir. 1988) (Aldisert, J., concurring). A number of district courts have indicated their agreement with this view,[9] as have the commentators. See page 15 & note 13, *infra*.

[8] The Solicitor General agrees (*Lebman* Am. Br. 6 n.5) that the Court has never "pass[ed] on the appropriateness of that practice." See also *Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990), slip op. 20-21; *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1387 (7th Cir. 1990), petition for cert. pending, 59 U.S.L.W. 3354 (filed Sept. 26, 1990) (No. 90-526); *In re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1539 (3d Cir.) (en banc), cert. denied, 488 U.S. 849 (1988).

[9] See *Welch* v. *Cadre Capital*, 735 F. Supp. 467, 474, 477, 482 (D. Conn. 1990); *Robertson* v. *Deloitte, Haskins & Sells*, 732 F. Supp. 979, 985 (E.D. Ark. 1990); *Dingler* v. *T.J. Raney & Sons, Inc.*, 708 F. Supp. 1044, 1055 (W.D. Ark. 1989); *Kayne* v. *Paine-Webber Inc.*, 703 F. Supp. 1334, 1343 (N.D. Ill. 1989); *Bernstein* v. *Crazy Eddie, Inc.*, 702 F. Supp. 962, 980-981 (E.D.N.Y. 1988), vacated in part on other grounds, 714 F. Supp. 1285 (1989); *Marchese* v. *Nelson*, 700 F. Supp. 522, 523 (D. Utah 1988); *Bath* v. *Bushkin, Gaims, Gaines & Jonas*, 695 F. Supp. 1156, 1159-1162 (D. Wyo. 1988), aff'd in part & rev'd in part, 913 F.2d 817, 818-819 (10th Cir. 1990) (panel bound by circuit precedent to apply state limitations period). See also *Elysian Fed. Sav.* v. *First Interregional Equity*, 713 F. Supp. 737 (D.N.J. 1989) (following *Data Access*).

These opinions cogently demonstrate the appropriateness of applying a federal limitations period. Indeed, the structure, history, and policies of the federal securities laws present a compelling case for borrowing a federal statute of limitations for the implied 10(b) cause of action. Even without such indicia of congressional intent, moreover, the same conclusion would be required under the Court's decisions in *Agency Holding* and *DelCostello*, which recognize the need for a federal limitations period " 'when a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking' " (483 U.S. at 148, quoting 462 U.S. at 171-172). Resort to state limitations periods in 10(b) actions has produced a morass of inconsistency, unpredictability, and inefficiency. Only application of a federal statute of limitations can achieve the necessary certainty and uniformity in this important area and effectuate the policy choices that Congress carefully made in enacting the federal securities laws.

A. Absorption Of State Limitations Periods For 10(b) Actions Has Led To Inconsistency, Unpredictability, And Wasteful Litigation

In borrowing state limitations periods in 10(b) actions, courts were heavily influenced by "historical habit" developed in other areas of law (*Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 456 (3d Cir. 1979) (Sloviter, J., concurring)) and acted largely "on auto-pilot, without discussing whether something differentiated securities laws from other statutes." *Short*, 908 F.2d at 1387. "There are, however, no strong policy reasons for borrowing state statutes of limitations with respect to implied claims arising under federal [securities] law." 4 A. Bromberg & L. Lowenfels, SECURITIES FRAUD & COMMODITIES FRAUD § 11.9(300), at

11:205 (1989). This reflexive approach has resulted in "one tottering parapet of a ramshackle edifice" in which "the courts of appeals disagree on every possible question about limitations periods in [10(b)] securities cases." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987).

The widespread disagreements among the courts were recently cataloged by the American Bar Association Committee on Federal Regulation of Securities. See *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 BUS. LAW. 645 (1986).[10] To begin with, courts disagree on what state law is most analogous to 10(b) actions. Different courts have borrowed the limitations period for common law fraud suits, for violations of the state blue sky law, and even for personal injury litigation. *Id.* at 648, 650-652, 659-666. Several circuits or states have yet to resolve the issue of the applicable limitations period. *Id.* at 646, 659-666. Other courts have established different rules for the various states in the circuit, applying the fraud period for 10(b) actions in one state and the blue sky period for identical suits in another state. *Id.* at 660. And some courts have declined to adopt a controlling rule of law at all, electing instead to decide on a case-by-case basis which state cause of action is most analogous to the 10(b) claim presented in the particular suit. *Id.* at 651-652. As a result, the limitations period applicable to 10(b) actions ranges anywhere from one year to 10 years, and in some circuits is simply indeterminate. *Id.* at 646, 650.

These inconsistencies, serious as they are, do not represent the full extent of the problem. For example, even

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[10] A circuit-by-circuit and state-by-state summary of the law is contained in an appendix to the Report (41 BUS. LAW. at 659-666) and was updated in the Solicitor General's *amicus* brief in this Court in *Lebman*. Bromberg and Lowenfels devote some 100 pages in their treatise to the complexities of statutes of limitations in federal securities cases.

circuits that have adopted a single standard for determining the state statute of limitations to be borrowed (*e.g.*, the statute of limitations for fraud) in fact are forced to apply different limitations periods because of variations in the laws of the respective states; state fraud statutes of limitations range from two to 10 years, while state blue sky laws vary from one to three years. ABA Report at 650. Further complications arise when states have more than one fraud or blue sky limitations period and when they amend their laws (or reinterpret them in judicial decisions) in ways that affect the selection of the most appropriate analogy for 10(b) actions. *Id.* at 652-653; *Short*, 908 F.2d at 1388-1389. Thus, as the Second Circuit recently observed, "there is no uniformity in either the type of state limitations statute from which the federal courts borrow or the periods provided by the states for a given category of action." *Ceres Partners*, slip op. 13.

Other sources of confusion and conflict arise from the "difficult questions [that are presented] concerning whose tolling and estoppel doctrines apply: the state's, the federal court's, or both?" *Short*, 908 F.2d at 1389. Courts generally have followed federal rules for tolling and estoppel, although that approach is open to serious doubt after this Court's decisions in *Tomanio* (446 U.S. at 483-486) and *Johnson* v. *Railway Express Agency* (421 U.S. 454, 463-464 (1975)), which recognize that federal law borrowing a state statute of limitations also incorporates state tolling rules. See *Norris*, 818 F.2d at 1331. What is more, federal courts do not apply the tolling and estoppel rules consistently, disagreeing, for instance, on whether a subjective or objective standard governs the plaintiff's due diligence obligation and the effect of a defendant's active concealment of his fraud. See ABA Report at 654-655.[11]

[11] As the Report also notes (at 655), "[m]ore troubling than the complexity of the tolling issue, however, is the inescapable conclusion that Congress did not intend equitable tolling to apply in actions under the securities laws." This issue is further discussed at pages 33-34, 42-43, *infra*.

The practical consequences of these legal conflicts are both plain and severe. First, neither plaintiffs nor defendants can ascertain their legal rights with any confidence. This is conducive to nothing but uncertainty and unfairness, as plaintiffs unwittingly lose claims they thought they had and defendants are unable to put past events behind them and reliably plan for the future. It also spawns extensive and wasteful litigation to resolve limitations issues wholly collateral to the merits of the underlying dispute. See *Owens* v. *Okure*, 488 U.S. at 239-240, 245-247; *Agency Holding*, 483 U.S. at 150; *Wilson*, 471 U.S. at 275. This "situation is a nightmare" to which "[l]awyers and courts alike devote untold hours." *Short*, 908 F.2d at 1389.[12] Such costs are especially unjustified here, for " '[f]ew areas of the law stand in greater need of firmly defined, easily applied rules than does the subject of periods of limitations.' " *Wilson*, 471 U.S. at 266, quoting *Chardon* v. *Fumero Soto*, 462 U.S. 650, 667 (1983) (Rehnquist, J., dissenting).

Furthermore, application of state limitations periods leads to divergent outcomes depending entirely upon the state where plaintiff files suit. Such discrepancies in the rights of the parties are inherently inequitable and cannot be reconciled with the nationwide scope of the country's securities markets and federal securities laws. As the Third Circuit explained in *Data Access* (843 F.2d at 1549):

> The necessity for uniform federal remedies in security cases would seem to demand recourse to a uniform federal statute of limitations. A broker in New York, an issuer in Delaware, a purchaser in San Francisco, an accountant in New Jersey, and a lawyer in Pennsylvania should be subject to the same statute of limitations for actions based on section 10(b) or Rule 10b-5.

[12] In this very case, more than four years—the entire life of the lawsuit—have been devoted to resolving the limitations question.

See also *Ceres Partners*, slip op. 12 ("federal securities regulation is inherently national in scope and in need of uniform rules").

Equally problematic, variation in the applicable limitations period improperly encourages forum shopping by plaintiffs. This is a particular concern under the federal securities laws, which authorize nationwide service of process and contain broad venue provisions that allow suit to be brought in any district where "the defendant is found or is an inhabitant or transacts business" or where the transaction or violation took place. 15 U.S.C. §§ 77v(a), 78aa. See L. Loss, FUNDAMENTALS OF SECURITIES REGULATION 993 (2d ed. 1988). Thus, if state statutes of limitations are followed, plaintiffs will be afforded an undue opportunity to sue whenever the limitations period in a single available jurisdiction has not run, even though the time in all other relevant jurisdictions—including those that have the most substantial connections to the transaction and litigation—has lapsed. This problem is especially acute, and the sound judicial management of litigation especially difficult, in the common situation of nationwide or multi-state class actions. See *Short*, 908 F.2d at 1389.

In sum, as the ABA Report concludes (at 646, 647), the borrowing of state limitations periods in 10(b) suits has created "serious problems" and resulted in a "disarray" that

> serves no public purpose. This uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of the parties litigating identical claims in different states. Neither plaintiffs nor defendants can determine their rights with any certainty. Vast amounts of judicial time and attorneys' fees are wasted. Moreover, managements of publicly held companies, as well as their auditors and attorneys, are frequently unable to assess the impact of possible litigation under rule 10b-5. This deprives investors of information adequate for informed evaluation of such companies' potential liabilities.

Accordingly, "the use of state law has disserved not only the federal courts but litigants, the bar, and the investment community." *Id.* at 656. The current "state of the law * * * [is] chaotic" and "deference to state law is not warranted because federal, not state, interests are involved." *Ibid.*

In the face of this impenetrable thicket, "[l]oud calls for reform issue from scholars and the bar. With a unanimity unmatched in any other corner of securities law, everyone wants a simpler way—and to everyone that means a uniform federal statute of limitations." *Short*, 908 F.2d at 1389. As the ABA Report noted (at 647), the "obvious" way to obtain a uniform statute is "to look to the limitations periods Congress provided for the express private rights of action under the securities laws." Professor Loss has explained the soundness of such an approach:

> [W]ith the 1933 and 1934 Acts so closely related, why not look to *their* statutes of limitations by way of analogy rather than to a variant state law? Would it not be eminently more consistent with the overall statutory scheme to look to what Congress itself did when it was thinking specifically of private actions in securities cases rather than to a grab-bag of more or less analogous state statutes?

Loss, *supra*, at 994-995 (emphasis in original). On this proposal "the commentators seem to be of one view." *Id.* at 996.[13]

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[13] In addition to the SEC and the ABA Federal Securities Regulation Committee, both of which agree that a uniform federal limitations period is appropriate, see also, *e.g.*, A. Bromberg, SECURITIES LAW: SEC RULE 10b-5, § 12.9, at 284 (1967); 4 Bromberg & Lowenfels, *supra*, § 11.9(500); Bateman & Keith, *Statute of Limitations Applicable to Private Actions under SEC Rule 10b-5: Complexity in Need of Reform*, 39 MO. L. REV. 165, 183 (1974); Block &

(Footnote continued on following page)

As we now show, the structure, history, and policies of the federal securities laws, as well as this Court's recent decisions, compel the conclusion that the commentators have universally endorsed: 10(b) actions should be subject to a uniform limitations period drawn from the express limitations periods in the federal securities laws.

[13] *continued*

Barton, *Statute of Limitations in Private Actions Under Section 10(b)—A Proposal for Achieving Uniformity*, 7 SEC. REG. L.J. 374, 381-382 (1980); Bloomenthal, *Statutes of Limitations and the Securities Acts—Part II*, 7 SEC. & FED. CORP. L. REP. 25, 25-26, 30 (Apr. 1985); Fiebach & Doret, *A Quarter Century Later—The Period of Limitations for Rule 10b-5 Damage Actions in Federal Courts Sitting in Pennsylvania*, 25 VILLANOVA L. REV. 851, 879-880 (1979-80); Israels, Book Review, 77 YALE L.J. 1585, 1591-1592 (1968); Kaulbach, *A Functional Approach to Borrowing Limitations Periods for Federal Statutes*, 77 CALIF. L. REV. 133, 135-136, 160, 162-165 (1989); Martin, *Statutes of Limitation in 10b-5 Actions: Which State Statute is Applicable?*, 29 BUS. LAW. 443, 454-458 (1974); Raskin & Enyart, *Which Statute of Limitations in a 10b-5 Action?*, 51 DENVER L.J. 301, 302 (1974); Ruder, *Civil Liability Under Rule 10b-5: Judicial Revision of Legislative Intent?*, 57 NW. L. REV. 627, 649-650, 681 n.43 (1962); Ruder & Cross, *Limitations on Civil Liability under Rule 10b-5*, 1972 DUKE L.J. 1125, 1144, 1148-1150; Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 WAYNE L. REV. 635, 638, 643 (1967); Comment, *Securities*, 13 CREIGHTON L. REV. 1436, 1449 (1980); Comment, *A Cry for Help: The Ninth Circuit and the Statute of Limitations in Rule 10b-5 Actions*, 22 U.C.L.A. L. REV. 947, 950-951, 963 (1975); Note, *Obtaining Uniformity for Section 10(b) and Rule 10b-5 Causes of Action*, 22 CONN. L. REV. 525, 526, 534-538, 559-562 (1990); Note, *The Proper Statute of Limitations on a Rule 10b-5 Action*, 23 IND. L. REV. 731, 739-741, 749-751 (1990); Note, *Securities Regulation—Statutes of Limitations*, 19 SETON HALL L. REV. 724, 725, 752-753 (1989); Note, *Securities Litigation—Statutes of Limitations*, 34 VILLANOVA L. REV. 611, 612-613, 626-629 (1989); Note, *Statutes of Limitation for Section 10(b) and Rule 10b-5: A New Proposal for Uniformity*, 46 WASH. & LEE L. REV. 665, 666, 674, 683-687 (1989).

B. The Structure, History, And Policies Of The 1933 And 1934 Acts Demonstrate That A Federal Statute Of Limitations Should Apply To 10(b) Actions

The legislative development of the 1933 and 1934 Acts constitutes direct evidence of Congress's intent and demonstrates that the implied 10(b) cause of action should be subject to a federal statute of limitations drawn from the express limitations periods provided in the federal securities laws. The specifics of this history are most relevant to the question of *which* federal limitations periods should be borrowed for 10(b) actions, and accordingly a detailed discussion is deferred to Section II, *infra*. At this point, three general observations suffice to demonstrate that application of a federal rather than a state limitations period is the only approach consistent with the statutory scheme adopted by Congress. See *Ceres Partners*, slip op. 28-29 ("judicial selection of a uniform nationwide limitations period is what Congress would have intended for private rights of action judicially implied under [the federal securities laws]").

First, the limitations issue in this case must be viewed against the background fact that 10(b) suits involve a *judicially implied* cause of action. See, *e.g.*, *Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 477 (1977); *Blue Chip Stamps*, 421 U.S. at 729-730.[14] In that circumstance, congressional silence concerning the applicable statute of limitations does not even arguably suggest an understanding that state limitations periods would be incorporated. Con-

[14] Although the Court has accepted the existence of an implied 10(b) cause of action, recent decisions make it doubtful that an implied action would be recognized if the issue arose for the first time today. See, *e.g.*, *Karahalios* v. *National Fed. of Federal Emp., Local 1263*, 109 S. Ct. 1282, 1286, 1288 (1989); *Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 578 (1979); *Thompson* v. *Thompson*, 484 U.S. 174, 188 (1988) (O'Connor, J., concurring); *id.* at 190 (Scalia, J., concurring in the judgment); *Carlson* v. *Green*, 446 U.S. 14, 39-40 n.5 (1980) (Rehnquist, J., dissenting).

gress's failure to supply a limitations period for a right of action that it did not enact, but that subsequently was implied by the courts, is hardly surprising and reveals no intent by Congress to absorb state law. See page 20 note 17, *infra*.

Second, and of critical significance, Congress has not been silent about the applicability of federal statutes of limitations to the federal securities actions that it did create. On the contrary, *every* private cause of action explicitly provided in the 1933 and 1934 Acts was accompanied by an *express* limitations period.[15] And, as discussed in detail

[15] In brief, Section 11 of the 1933 Act (15 U.S.C. § 77k) provides an express private cause of action for untrue statements or material omissions in registration statements, and Section 12 (15 U.S.C. § 77*l*) provides an action for untrue statements or material omissions in the sale of securities; both are subject to the one-year/three-year limitations provision in Section 13 (15 U.S.C. § 77m). Section 9(e) of the 1934 Act (15 U.S.C. § 78i(e)) provides an express cause of action for false or misleading statements or actions to manipulate security prices, Section 18 (a, c) (15 U.S.C. § 78r(a, c)) for false or misleading statements in any application, report, or document filed with the SEC, and Section 29(b) (15 U.S.C. § 78cc(b)) for rescission of certain transactions that violate the 1934 Act or rules thereunder; all of these causes of action provide their own one-year/three-year limitations period. (The limitations period for Section 29(b) was added in 1938, see *Data Access*, 843 F.2d at 1545.)

The only exception to this consistent pattern of one-year/three-year limitations periods for the express actions in the 1933 and 1934 Acts is the "short-swing profit" provision in Section 16(b) of the 1934 Act (15 U.S.C. § 78p(b)). Like the other provisions in those Acts, Section 16(b) is subject to an express limitations period, the specified period, however, is two years. In contrast to the above provisions of the Acts (and to Section 10(b)), which are compensatory and remedial in nature, Section 16(b) is strictly a deterrent and prophylactic. See *Ceres Partners*, slip op. 32-33; *Data Access*, 843 F.2d at 1546; Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 WAYNE L. REV. 635, 638 (1967). Because of its distinctive character, Section 16(b) does not provide an apt analogy to 10(b) actions for purposes of the statute of limitations. A similar deterrent cause of action, which also contains an explicit limitations period but of five years, was adopted in the Insider Trading and Securities Fraud Enforcement Act of 1988 and is discussed at pages 38-41, *infra*.

below (see pages 24-25, *infra*), those explicit causes of action are quite analogous to 10(b) actions. Given that Congress consistently provided a federal limitations period for each express statutory action, it would be completely inconsistent with the structure of the Acts—and indeed would defy common sense—for the courts to create a contrary rule imposing state limitations periods on the judicially implied 10(b) cause of action. See *FBI* v. *Abramson*, 456 U.S. 615, 625 n.7 (1982) (citation omitted) ("our duty then is 'to find that interpretation which can most fairly be said to be imbedded in the statute, in the sense of being most harmonious with its scheme and with the general purposes that Congress manifested' ").[16]

Third, the express federal limitations periods enacted by Congress serve important federal policies and embody a deliberate congressional balance between the interests of repose and enforcement. As this Court has emphasized, 10(b) litigation "presents a danger of vexatiousness different in degree and in kind from that which accompanies litigation in general," and "Congress itself recognized the potential" for such abuses when it enacted the 1933 and 1934 Acts. *Blue Chip Stamps*, 421 U.S. at 739, 740. With particular respect to the issue of limitations, the legislative history establishes that Congress specifically concluded that a period longer than the one-year/three-year statute

[16] Indeed, directly indicating Congress's understanding that federal causes of action should be subject to federal limitations periods, Senator Norris explained that "[r]unning all through the statutes we pass—criminal statutes and civil statutes—there is a statute of limitations. Everyone concedes that it is a wise thing to have a statute of limitations." 78 Cong. Rec. 8199 (1934). See also *Stock Exchange Practices: Hearings on S. Res. 84, S. Res. 56, & S. Res. 97 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st. Sess. 7561 (1934) (statement of Roland L. Redmond, Attorney, New York Stock Exchange) (referring to the "absurd" situation if "local practices with regard to limitations might result in varied rules of law as to the liability * * * in the Federal courts").

of repose was unnecessary and presented too great a danger of business disruption and abusive litigation. See pages 28-36, *infra*. By contrast, "State legislatures do not devise their limitations periods with national interests in mind." *Wilson*, 471 U.S. at 269 n.18. See also *Burnett* v. *Grattan*, 468 U.S. 42, 51-53 (1984). Since Congress carefully designed the Acts to avoid the problem of untimely lawsuits, it would be entirely inappropriate for courts to discard the expressly prescribed federal limitations and open up implied 10(b) actions to state periods that are both longer and subject to equitable tolling. See, *e.g.*, *Miles* v. *Apex Marine Corp.*, No. 89-1158 (U.S. Nov. 6, 1990), slip op. 12 ("[i]t would be inconsistent with our place in the constitutional scheme were we to sanction more expansive remedies in a judicially-created cause of action * * * than Congress has allowed in [express actions]"); *Blue Chip Stamps*, 421 U.S. at 736 ("[i]t would indeed be anomalous to impute to Congress an intention to expand * * * [liability under] a judicially implied cause of action beyond the bounds it delineated for comparable express causes of action").

C. Recent Decisions Of This Court Make Clear That A Federal Statute Of Limitations Should Apply To 10(b) Actions

Application of a federal statute of limitations to 10(b) actions is required not only by the structure, history, and policies of the securities laws, but also by the recent decisions of this Court in *Agency Holding*, *Wilson*, and *DelCostello*. These cases have recognized the applicability of federal rather than state limitations periods in circumstances similar to those presented here.[17]

[17] In *DelCostello*, the Court recognized that the generally applicable limitations analysis "makes more sense as applied to a cause of action expressly created by Congress than as applied to one

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The *Agency Holding* analysis directs courts to borrow a federal statute of limitations when " 'federal law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that [federal] rule * * * significantly more appropriate.' " 483 U.S. at 148, quoting *DelCostello*, 462 U.S. at 171-172. This standard entails a three-part inquiry: (1) "whether all claims arising out of the federal statute 'should be characterized in the same way' " and thus be subject to a single type of limitations statute, or " 'whether they should be evaluated depending upon the varying factual circumstances and legal theories presented in each individual case' " (483 U.S. at 147, quoting *Wilson*, 471 U.S. at 268); (2) whether the federal or state statute "offers the close[r] analogy" to the cause of action at issue (483 U.S. at 150); and (3) whether the "federal policies at stake and the practicalities of litigation" make the federal limitations period "more appropriate" (*id.* at 153). This analysis demonstrates that a federal statute of limitations is applicable to 10(b) actions.

[17] *continued*
found by the courts to be implied in a general statutory scheme—especially when that general statutory scheme itself contains a federal statute of limitations for a related but separate form of relief." 462 U.S. at 158 n.12. Where Congress has failed to provide a limitations period for an express cause of action, the Court generally has followed "a sort of fallback rule of thumb" that "prefer[s] * * * borrowing state limitations periods" based "on the assumption that, absent some sound reason to do otherwise, Congress would likely intend that the courts follow their previous practice of borrowing state provisions." *Ibid.* This reasoning is simply inapplicable where, as here, a judicially implied rather than a congressionally prescribed cause of action is involved and Congress in fact provided a federal limitations period for every express statutory action it enacted. See *United Parcel Service, Inc.* v. *Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring in the judgment).

1. A Single Characterization Of 10(b) Claims Is Most Appropriate

As with the civil RICO action in *Agency Holding*, a single characterization of 10(b) claims is most appropriate. Like RICO, 10(b) claims " 'encompass numerous and diverse topics and subtopics.' " *Agency Holding*, 483 U.S. at 149 (citation omitted). "[S]ection 10(b) and Rule 10b-5 embrace a galaxy of actions" (*Data Access*, 843 F.2d at 1543), including suits (as the government explained in its *amicus* brief in *Lebman* (at 10)) that are "readily * * * analog[ous] to actions for common law fraud, breach of contract, breach of fiduciary duty, misappropriation, and violation of blue sky laws, among others." Each of these state claims provides a statute of limitations that is a potential candidate for borrowing in 10(b) actions. Furthermore, like RICO, 10(b) actions were " 'unknown to common law' " (*Agency Holding*, 483 U.S. at 150 (citation omitted)) and " 'have no precise counterpart in state law' " (*Owens* v. *Okure*, 488 U.S. at 248 (citation omitted)). See page 23, *infra*. In these circumstances, any requirement that every individual 10(b) suit be properly matched to one among the multiplicity of possible state law choices would cause "intolerable 'uncertainty and time-consuming litigation.' " *Agency Holding*, 483 U.S. at 150, quoting *Wilson*, 471 U.S. at 272.

2. Federal Rather Than State Law Provides The Closer Analogy To 10(b) Actions

In selecting the appropriate limitations period, the express provisions of the federal securities laws offer a closer analogy to 10(b) actions than do state laws. Indeed, the irreconcilable conflict among the circuits over the proper state limitations statute to borrow (see pages 11-15, *supra*) is proof positive of the intractable difficulty of relying on state law analogies.

As this Court has recognized, "[a]ctions under Rule 10b-5 are distinct from common-law deceit and misrepresentation claims." *Basic Inc.* v. *Levinson*, 485 U.S. 224, 244 & n.22 (1988). See, *e.g.*, *Herman & MacLean* v. *Huddleston*, 459 U.S. at 390 (common-law fraud standard of clear and convincing evidence not applicable to 10(b) claims); *Blue Chip Stamps*, 421 U.S. at 744 (purchaser/seller requirement applicable under Section 10(b) but not under common-law fraud). In fact, modern securities markets and practices fundamentally "differ from the face-to-face transactions contemplated by early fraud cases" (*Basic*, 485 U.S. at 243-244), and "the typical fact situation in which the classic tort of misrepresentation and deceit evolved was light years away from the world of commercial transactions to which Rule 10b-5 is applicable." *Blue Chip Stamps*, 421 U.S. at 744-745. Accordingly, "far from being a mirror image or a reasonable facsimile of common law fraud, actions brought under section 10(b) and Rule 10b-5 appear to be *sui generis*." *Data Access*, 843 F.2d at 1545.

Likewise, state blue sky laws do not provide an apt analogy to 10(b) actions. Such state laws "come[ ] in a variety of shapes and sizes" (Loss, *supra*, at 877) and frequently differ both from one another and from federal law. For example, some blue sky laws protect only purchasers and not sellers of securities, some fail to establish liability for secondary participants (such as accountants and attorneys) who assist a wrongdoing seller, and some fail to provide a damages remedy for violations. See *Data Access*, 843 F.2d at 1544. Given the limited nature of and variations among these provisions, state blue sky laws do not offer a close analogy to 10(b) actions.

By contrast, the express causes of action in the federal securities laws are quite similar to 10(b) claims. See page 18 note 15, *supra*. These explicit provisions of the 1933 and 1934 Acts were, of course, enacted contemporaneous-

ly with Section 10(b) and, as the immediate context in which Section 10(b) was drafted and passed, offer a revealing insight into the proper application of that section and the general securities law policies that Congress adopted.

Just as the civil RICO provision "was patterned after" the Clayton Act (*Agency Holding*, 483 U.S. at 150), which led the Court to borrow the Clayton Act's statute of limitations for RICO actions, the 10(b) remedy bears a close resemblance to several of the express liability provisions of the 1933 and 1934 Acts. For example, Sections 11 and 12 of the 1933 Act (15 U.S.C. §§ 77k, 77*l*), and Sections 9(a) and 18(a) of the 1934 Act (15 U.S.C. §§ 78i(a), 78r(a)), establish express causes of action (and are subject to an express statutory limitations period) against a defendant who makes an "untrue statement of a material fact" or omits "to state a material fact * * * necessary to make the statement[ ] * * * not misleading."[18] In the same fashion, Section 10(b) forbids the use of any "manipulative or deceptive device or contrivance" in connection with a sale of securities, and Rule 10b-5 renders it unlawful "[to] make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading." 15 U.S.C. § 78j(b); 17 C.F.R. § 240.10b-5. Furthermore, as this similarity in language would suggest, Section 10(b) and the express causes of action in the 1933 and 1934 Acts "are aimed at the same objectives," "aim to compensate the same type of injury," and "are designed to fill a void in the common law and to create remedies that would be uniform throughout our nation's commercial universe." *Data Access*, 843 F.2d at 1548-1549.

[18] Section 9 of the statute provides a cause of action against a defendant who either "creat[es] a false or misleading appearance of active trading" (§ 9(a)(1)) or "make[s] * * * any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact" (§ 9(a)(4)).

Thus, "the securities acts are addressed to the conduct at stake in this case—securities fraud"; "in particular, [Section 12] covers the express right of action * * * [for] incorrect statements and material omissions in the course of selling securities"—precisely the type of conduct plaintiffs have alleged here. *Short*, 908 F.2d at 1388. It is these explicit causes of action in the federal securities laws, not state fraud or blue sky laws, that constitute the proper analogy to 10(b) actions.

3. Federal Securities Policies And The Practicalities Of Litigation Support Application Of A Uniform Federal Limitations Period

The policies of the federal securities laws and the practicalities of securities litigation also support application of a uniform federal limitations period in 10(b) actions. As noted above (see pages 17-20, *supra*), Congress's enactment of a federal regulatory scheme, and its inclusion of a statute of limitations for every express action it created, demonstrate the important federal policy of having uniform limitations periods in securities cases.

The "practicalities" of 10(b) litigation provide additional "compelling reasons" for a uniform federal limitations period. *Agency Holding*, 483 U.S. at 153. Absent such federal uniformity, 10(b) actions would be governed by a variety of state statutes of limitations that range from one to 10 years. See pages 11, 13-14, *supra*. As with civil RICO, such a patchwork of "state statutes would present the danger of forum shopping and, at the very least, would 'virtually guarante[e] * * * complex and expensive litigation over what should be a straightforward matter.' " *Id.* at 154 (citation omitted). This concern is particularly substantial in

light of the liberal venue and service-of-process provisions in the federal securities laws. See page 14, *supra*.

In addition, the federal securities laws were intended to provide uniform regulation of nationwide markets. See, *e.g.*, 15 U.S.C. § 78b. And, like civil RICO, "some nexus to interstate or foreign commerce is required as a jurisdictional element of a [10(b)] claim"; indeed, 10(b) cases "commonly involve interstate transactions" so that "the statute of limitations of several States could govern any given [10(b)] claim." *Agency Holding*, 483 U.S. at 153-154. Given the "multi-state nature" of 10(b) suits (*id.* at 154), the overarching interest in uniformity weighs heavily in favor of a federal limitations period.

Finally, the existing legal disarray in the applicable statute of limitations generates needless confusion in the business and financial communities and wasteful litigation in the federal courts. See pages 11-15, *supra*. "Congress intended the identification of the appropriate statute of limitations to be an uncomplicated task for judges, lawyers, and litigants, rather than a source of uncertainty, and unproductive and ever-increasing litigation." *Wilson*, 471 U.S. at 275. Such "uncertainty is costly to all parties," depriving plaintiffs of their "just remedy" if they incorrectly predict the applicable period and denying defendants both the ability to "calculate their contingent liabilities" and the peace of mind of "knowing with confidence when their delicts lie in repose." *Id.* at 275 n.34. Thus, as the Court has recognized in other areas, "[t]he federal interests in uniformity, certainty, and the minimization of unnecessary litigation all support the conclusion" (*id.* at 275) that the implied 10(b) cause of action should be subject to a uniform federal limitations period drawn from the express statutes of limitations in the federal securities laws.

II. THE APPROPRIATE FEDERAL LIMITATIONS PERIOD FOR 10(b) ACTIONS IS THE ONE-YEAR/THREE-YEAR PROVISION IN THE 1933 AND 1934 ACTS

The federal securities laws contain two limitations periods that have been suggested as appropriate for borrowing in private 10(b) actions. In our view, the applicable federal statute of limitations is the one-year/three-year provision in the 1933 and 1934 Acts. The SEC, on the other hand, has proposed the five-year provision in the Insider Trading and Securities Fraud Enforcement Act of 1988 ("ITSFEA").

All three of the cases that have considered these two federal limitations periods have adopted the one-year/three-year-rule.[19] A careful examination of the structure, history, and policies of the 1933 and 1934 Acts and the ITSFEA demonstrates that this conclusion plainly is correct.

In enacting the 1933 and 1934 securities laws, Congress specifically determined that a five-year limitations period was too long and would invite unfounded and abusive litigation. Accordingly, for all but one of the express statutory causes of action—actions closely analogous to the 10(b) action subsequently implied by the courts—Congress deliberately crafted the one-year/three-year provision to bar lawsuits that it considered untimely and undesirable.

This congressional determination is controlling here. It is the contemporaneous legislation on which 10(b) actions ultimately rest, not the ITSFEA enacted decades later, that informs the appropriate limitations period for such implied suits under the 1934 Act. See *Touche Ross & Co.*

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[19] See *Ceres Partners*, slip op. 29-37, aff'g 714 F. Supp. 679, 684-685 (S.D.N.Y. 1989); *Short*, 908 F.2d at 1390-1392; *Elysian Fed. Sav.*, 713 F. Supp. at 742-745; see also *Data Access*, *supra* (adopting the one-year/three-year limitations period prior to enactment of ITSFEA).

v. Redington, 442 U.S. at 574-575 n.16 ("[g]iven the fact that our task is to discern the intent of Congress when it enacted § 17(a) in 1934, we doubt the relevance of [subsequent legislation] to our inquiry"); see also *Universities Research Ass'n* v. *Coutu*, 450 U.S. 754, 778 (1981).

As the Seventh Circuit explained in *Short* (908 F.2d at 1390), "[a]ny court choosing a federal statute of limitations between 1946 (the date of the first decision recognizing a private right of action under Rule 10b-5) and 1988 necessarily would have selected the [one-year/three-year provision]."[20] It is thus anomalous for the SEC to assert that Congress in 1988, without any indication of an intent to do so, fundamentally revised the policies of the 1934 Act and retrospectively changed the limitations period that should have been applied for decades. In fact, contrary to the SEC's position, Congress specifically confined the ITSFEA to the unique problem of insider trading and expressly provided that the statute would *not* affect general 10(b) law. In these circumstances, it is the one-year/three-year limitations provision that the Court should apply in 10(b) actions.

A. In The 1933 And 1934 Acts, Congress Adopted An Outer Limitations Period Of Three Years And Specifically Rejected A Five-Year Period

The limitations provisions in the 1933 and 1934 Acts "have an extensive legislative history" that "is highly relevant to the assertion of implied claims, and strongly rebuts any intention on the part of Congress that implied

[20] The SEC concedes as much (*Lebman* Am. Br. 16): "when an implied right of action under Rule 10b-5 was first recognized more than forty years ago, the selection of those [express] limitations periods [in the 1933 and 1934 Acts] rather than state law arguably would have been the better solution."

claims should have a more liberal period of limitation than the remedies Congress expressly created." Bloomenthal, *The Statute of Limitations and Rule 10b-5 Claims: A Study in Judicial Lassitude*, 60 COLO. L. REV. 235, 258-259 (1989).

Starting with the Securities Act of 1933, Congress consistently has set forth an explicit federal limitations period for every express cause of action it has enacted. The original 1933 Act provided that any private civil actions must be brought within two years of the discovery of the violation and in no event more than 10 years after the violation. 48 Stat. 74 (1933). Congress recognized that a statute of limitations was necessary to prevent a plaintiff from "sleep[ing] on his rights"; without a limitations period, a plaintiff, "if the stock market was all right, could fail to proceed, or take no action, but if the stock market should subsequently turn unfavorable, then * * * [he would have] the opportunity to prosecute for fraud or the recovery of the purchase price." *Federal Securities Act: Hearing on H.R. 4314 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 1st Sess. 215 (1933) (statements of Rep. Thompson and Rep. Lea).

The ensuing Securities Exchange Act of 1934 was subject to "considerable organized and vocal opposition * * * fueled in part by a reaction to some of the civil liability provisions of the [1933] Securities Act." Bloomenthal, *supra*, 60 COLO. L. REV. at 260.[21] "As a result of the campaign waged by Wall Street and others against the Exchange Act, revisions were made both at the committee level (particularly in the House) and on the floor of the Senate to make the Act less objectionable to its critics." *Ibid.* See also *Blue Chip Stamps*, 421 U.S. at 753-754. As Senator Fletcher, the Senate floor manager, explained in

[21] On the legislative history, see also, *e.g.*, Bloomenthal, *supra*, Parts I & II, 7 SEC. & FED. CORP. L. REP. 17 (Mar. 1985), 25 (Apr. 1985); 4 Bromberg & Lowenfels, *supra*, § 11.9(200), at 11:203.

offering an amendment concerning the limitations provisions, "[t]he effort has been made to meet objections and criticisms and complaints which have come to the committee that the present act is too drastic," and "no objection has been raised to the amendment." 78 Cong. Rec. 8668 (1934).

In particular, significant changes were made in the limitations provisions in both the pending 1934 proposal and the existing 1933 Act, which was revised to conform to the 1934 Act. See 78 Cong. Rec. 8198, 8668, 8669 (1934); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 210. By providing a one-year/three-year limitations period in the amended Section 13 of the 1933 Act (which applied to actions under Sections 11 and 12) and in the express statutory action sections in the 1934 Act, Congress evidenced its clear intent that this period would govern private securities suits in general (absent a specific limitations provision to the contrary for a particular cause of action).

The original 1934 Senate bill provided that "[n]o action shall be maintained to enforce any liability created under [the express causes of action] unless brought within two years after the discovery of the facts constituting the violation [or the cause of action], nor unless brought within six years after such violation [or the cause of action accrued]." S. 3420, 73d Cong., 2d Sess. §§ 9(e), 18(c) (1934). The Senate Report generally noted the need "to give protection against 'strike' suits, or litigation brought in bad faith." S. Rep. No. 792, 73d Cong., 2d Sess. 18 (1934). The original House bill also contained an express statute of limitations, which, in contrast to the Senate version, provided that "[n]o action shall be maintained to enforce any liability created under this section unless brought within three years after the violation upon which it is based." H.R. 9323, 73d Cong., 2d Sess. §§ 8(e), 17(c) (1934); see also H.R. Rep. No. 1383, 73d Cong., 2d Sess. 21, 25 (1934).

These limitations provisions were the focus of extensive congressional consideration. In the Senate, Senator Fletcher introduced an amendment to reduce the two-year/six-year period to a one-year/five-year period on the ground that the original bill "allows too much leeway there." 78 Cong. Rec. 8197-8198 (1934). Senator King also repeatedly stated that the six-year period was "rather * * * long" and asked whether the committee had considered "limiting the period to 4 years or 3 years." *Id.* at 8198. Senator Norris agreed that six years was "too long." *Ibid.*

The Senate indicated its intention that the limitations period be "just and fair to both sides." 78 Cong. Rec. at 8200 (statement of Sen. Byrnes). It also expressed its general concern, however, about "blackmail suits * * * [and] purely contentious litigation." *Id.* at 8669 (statement of Sen. Fletcher).[22] As Senator Fletcher stressed, it was essential that "the person who made the misrepresentation or false statement ought to feel safe at some reasonable time that he will not be disturbed." *Id.* at 8198.

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[22] Concern over vexatious and baseless litigation repeatedly emerged in various contexts during the congressional hearings. See *Stock Exchange Regulation: Hearing on H.R. 7852 & H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. (1934) at 208 (statement of Richard Whitney, President, New York Stock Exchange) ("[i]t is obvious that provisions of this character will be productive of endless litigation and innumerable blackmail or 'strike' suits"), 303 (statement of Frank R. Hope, President, Association of Stock Exchange Firms) ("[t]he liabilities imposed are severe and would undoubtedly be used by unscrupulous purchasers, when they made an unfortunate purchase, as a means of forcing some settlement or contribution from the broker"); *Stock Exchange Practices: Hearings on S. Res. 84, S. Res. 56, & S. Res. 97 Before the Senate Comm. on Banking and Currency*, 73d Cong., 1st Sess. (1934) at 6633 (statement of Mr. Whitney) (same), 6909 (statement of Mr. Hope) (same), 6939 (statement of Alfred L. Burnheim, Twentieth Century Fund, Inc.) ("[a] provision of this sort invites blackmail and nuisance suits"), 6987 (statement of Eugene E. Thompson, President, Associated Stock Exchanges) ("the opportunity for blackmail is too apparent for safety").

Special concern was expressed that lengthy limitations periods "would deter men from serving on boards of directors" because of apprehension that their estates would be "liable * * * to * * * suit. * * * [W]e should bring to an end [their] fear, or the fear of [their] estate[s], of * * * suit." *Id.* at 8200 (statements of Sen. Byrnes).[23]

In addition, the Senate understood that an unduly lengthy limitations period would be undesirable and unfair because it would encourage plaintiffs to delay suit in order to speculate on the market: on the one hand, the plaintiff would benefit from the transaction if the market rose, and therefore would forgo litigation; on the other, he could sue if the market declined, thereby effectively treating the defendant as an insurer of his market speculation.

> [I]f a man buys something today and discovers tomorrow that some mistake has been made and perhaps he has a ground for suit because of fraud, under the terms of the bill he must bring his suit within 1 year. But suppose he thinks, "Perhaps the bonds I have bought will go up. I will not bring suit until I find out about that. If the bonds go down then I will have the option of suing these people and trying to recover. If the bonds go up, then I will not sue because I can get a profit on them.
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> * * * * *
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> [I]f he finds some technical mistake in the statement that has been put out, he might say to himself, "I have something that I can sue on if these bonds go down. If they go up I will not want to sue because I will get a profit on them, but should they go down, then I have the option of suing."

[23] See also William O. Douglas & G. Bates, *The Federal Securities Act of 1933*, 43 YALE L.J. 171, 195 (1933) ("The experience and judgment of men of affairs is of great value to most of our more important corporations. To deprive enterprises of this asset would seem uneconomic").

78 Cong. Rec. 8199 (1934) (statements of Sen. Kean). See *Blue Chip Stamps*, 421 U.S. at 747.[24]

The Senate specifically considered the objection that the amended one-year/five-year limitations period was "too short." 78 Cong. Rec. 8199, 8200 (1934) (statements of Sen. Norris and Sen. Adams). Of particular importance here in light of the SEC's position (see pages 43-44, *infra*), Senator Adams objected that "a limitation of a year is entirely inadequate" because "the plaintiff must prove that the false statement was willful." *Id.* at 8200. These criticisms were unavailing, however, and the Senate adopted the one-year/five-year limitations provision.

The Senate debates also make clear that this limitations provision imposed an absolute statute of repose that could not be extended on equitable grounds. As Senator Barkley explained:

> It really is not two limitations. If a man makes no discovery of fraud within the time limit of the statute then he cannot sue at all. The lapse of the 5 years * * * bars him from bringing suit at all where he has made the discovery. But if within that time he makes discovery of fraud and damage, then he is required to bring suit within 1 year after such discovery.
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> * * * * *

[24] See also *House Stock Exchange Regulation Hearing*, *supra*, at 303 (statement of Mr. Hope) ("They could engage in speculative purchases and could keep the benefits if the purchases turned out successful. If they were unsuccessful they could try to recover from their broker because of something they claimed they had heard him say, and if they could not recover, possibly force a settlement"), 307 (statement of Mr. Hope) (the statute is "particularly burdensome and puts tremendous advantages in the hands of a speculator to cover himself from bad speculation through endeavoring to force recovery from his broker for alleged misstatements"); *Senate Stock Exchange Practices Hearings*, *supra*, at 6565 (statement of Sen. Kean) ("[t]hey discover it after the market has gone down, and after something has happened, and they are looking for mistakes, and years afterward there is liability").

> [T]he 5-year limitation fixes the ultimate period of limitation when he can bring suit. But if a man discovers within 6 months, or 1 month, after he has been defrauded, that he has been defrauded—and he knows it just as well then as he would know it 3 years from that date—it does seem that he ought not to be allowed to let the whole period of the limitation run and within a week or two of its expiration bring suit on a transaction when he knew 4 years before that he had a right to sue.

78 Cong. Rec. 8198, 8200 (1934).[25] This fixed cutoff was expressly intended to prevent "blackmail." *Senate Stock Exchange Practices Hearings*, *supra*, at 6565 (statement of Sen. Kean); see also *id.* at 6566, 6718, 6993, 7561, 7743-7744. Thus, as the statutory language provides (15 U.S.C. § 77m) "[i]n no event" could suit be brought after the expiration of the outer time limit. The Solicitor General, courts, and commentators agree that this limitations provision is not subject to equitable tolling or estoppel.[26]

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[25] See also 78 Cong. Rec. at 8198 (statement of Sen. Fletcher) ("the time ought to be limited to 5 years"), *ibid.* (statement of Sen. Byrnes) ("a final limitation of 5 years"; "after 5 years * * * a suit may not be brought at all"); *ibid.* (statement of Sen. Norris) ("a final limit"); *ibid.* (statement of Sen. King) ("[s]uppose a person against whom a fraud was committed did not discover it until 6 years and 1 day [under the original bill]; then no action would lie"); *id.* at 8201 (statement of Sen. Barkley) ("After that 6-year period [under the original bill] he cannot bring suit. He might discover the fraud 5 years, 11 months and 29 days after it was committed, but he could still bring suit if he brought it on the thirtieth day, or on the first day after he made the discovery").

[26] See U.S. *Lebman* Am. Br. 14 n.17 ("The judicial consensus is that the three year outer limit of the Exchange Act one-and-three year limitations period is an absolute bar and is not subject to equitable tolling. * * * The legislative history of the Exchange Act confirms that Congress intended these periods to be absolute in order to ensure repose"); *Short*, 908 F.2d at 1391 ("[u]nless the 'in no event more than three' language cuts off claims of tolling and estoppel at three years, however, it serves no purpose at all"); *Norris*, 818 F.2d at 1332 ("[t]he legislative history in 1934 makes

(Footnote continued on following page)

The difference between the Senate's one-year/five-year limitations provision and the House's three-year provision was resolved at conference. Adopting the Senate's approach of a two-tier statute of repose but the House's outside time limit, the statute as enacted provides an express one-year/three-year statute of limitations. The conference committee made clear that this limitations provision is an absolute bar, "requir[ing] such suits to be brought within 1 year after the discovery of the facts constituting the violation and *in any event* within 3 years after such violation." H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. 32 (1934). See also *id.* at 36; 78 Cong. Rec. at 10,186 (statement of Sen. Byrnes) ("[T]he new laws will permit such a suit to be brought only within three years. * * * Under the new law, a suit must be brought within 3 years").

In summary, the following conclusions can be drawn from the legislative history of the 1933 and 1934 Acts. First, by applying the one-year/three-year provision to *all* private actions in *both* the 1933 and 1934 Acts (unless otherwise specifically provided), Congress expressed its intention that private litigation generally under these statutes would be subject to this limitations period. Second, Congress deliberately enacted a relatively short limitations provision, specifically reducing both the 10-year period contained in the original 1933 Act and the five-year period proposed in the 1934 Senate bill. Third, this short limitations period reflected a paramount federal policy requiring securities litigation to be brought promptly, in order to avoid unfair burdens and uncertainty for defendants, opportunistic litigation delays by plaintiffs, and

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[26] *continued*
it pellucid that Congress included statutes of repose because of fear that lingering liabilities would disrupt normal business and facilitate false claims"); ABA Report at 655 (drawing "the inescapable conclusion that Congress did not intend equitable tolling to apply in actions under the securities laws").

unwarranted and vexatious lawsuits in general. Fourth, the outer three-year period was designed to be an absolute maximum that prohibits suit from being brought for any reason after that date. Thus, as the Seventh Circuit has concluded, Congress enacted the express limitations provisions based on the "fear that lingering liabilities would disrupt normal business and facilitate false claims" (*Norris*, 818 F.2d at 1332) and the concern that "investors [not] gamble with other people's money" and benefit from "the wisdom given by hindsight." *Short*, 908 F.2d at 1392.

These propositions are fatal to the SEC's contention that a five-year limitations period should be applied in 10(b) actions. "[A]ttach[ing] more significance to a policy of repose than to protecting investors," Congress specifically rejected a five-year period as too long, and "selected with deliberation" a maximum three-year period instead. Bloomenthal, *supra*, 60 COLO. L. REV. at 262. Having enacted a one-year/three-year limitations provision for every express cause of action in the 1933 and 1934 Acts analogous to the subsequently implied 10(b) action, it is inconceivable that Congress would not have adopted the same provision for causes of action under Section 10(b); "[t]here can be little doubt that Congress would have imposed a similar policy of repose on an implied action based upon violation of section 10(b) and the rules adopted thereunder." *Ibid.*

B. The Insider Trading And Securities Fraud Enforcement Act Of 1988 Does Not Support Application Of A Five-Year Federal Limitations Period In 10(b) Actions

In the face of this overwhelming evidence of congressional intent, the SEC errs in asserting that the ITSFEA supports the borrowing of a five-year limitations provision in 10(b) actions. The government's position fails because (1) the private cause of action for insider trading

is not analogous to 10(b) suits in general; (2) Congress specifically limited the ITSFEA to insider trading suits and disclaimed any intention of affecting the law under Section 10(b) in other respects; and (3) unlike the absolute limitations periods expressly provided in the 1933 and 1934 Acts, the five-year provision in the ITSFEA apparently may be tolled on grounds of fraudulent concealment and equitable estoppel--an uncertain limitations protection that, as the SEC itself seems to recognize, Congress would not have intended for 10(b) suits.[27]

Because the ITSFEA is modeled on the Insider Trading Sanctions Act of 1984 ("ITSA"), we begin with a brief overview of the 1984 statute. As its title suggests, this Act was Congress's response to the escalating problem of insider trading. In particular, it authorizes the SEC to bring suit in such cases for "a civil penalty." Unlike a plaintiff's out-of-pocket damages in a private securities case—which in modern class action litigation can reach tens or even hundreds of millions of dollars—this carefully circumscribed civil penalty is based on "the profit gained or loss avoided" by the defendant and "shall not exceed three times" that amount. 15 U.S.C. § 78u-1(a)(2).[28] The purpose of the Act was to deter and punish violations, not to compensate investors. H.R. Rep. No. 355, 98th Cong., 1st Sess. 2 (1983).

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[27] It has consistently been held that in "cases relating to implied causes of action, the Court has understandably not invoked the 'administrative deference' rule" to give special weight to the views of the SEC. *Piper* v. *Chris-Craft Industries*, 430 U.S. 1, 41 n.27 (1977).

[28] The relevant provisions of the ITSA (which initially were codified in Section 21(d)(2) of the Securities Exchange Act of 1934) were recodified verbatim by the ITSFEA as Section 21A of the 1934 Act. Compare 15 U.S.C. § 78u-1 (1988) with 15 U.S.C. § 78u(d)(2) (Supp. IV 1986); see also H.R. Rep. No. 910, 100th Cong., 2d Sess. 35, 37 (1988). Citations in this brief to the ITSA refer to the statute as recodified in 1988 and currently in effect.

The ITSA further provides that "[n]o action may be brought under this section more than five years after the date of the purchase or sale." 15 U.S.C. § 78u-1(d)(5). See H.R. Rep. No. 355, at 12, 17. The legislative history explains that the "five-year statute of limitations for penalty actions * * * conforms to the five-year statute of limitations for criminal violations of the Securities Exchange Act." *The Insider Trading Sanctions Act of 1983: Hearing on H.R. 559 Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs*, 98th Cong., 2d Sess. 28 (1984) (statement of SEC Chairman John S.R. Shad).[29] While SEC civil injunctive actions generally are not subject to a statute of limitations (see page 4 note 2, *supra*), a limitations period was thought appropriate in this Act because of the "treble penalty" provided, and the SEC did not oppose inclusion of the limitations provision. *Insider Trading Sanctions and SEC Enforcement Legislation: Hearing on H.R. 559 Before the Subcomm. on Telecommunications, Consumer Protection, and Finance of the House Comm. on Energy and Commerce*, 98th Cong., 1st Sess. 57 (1983) (statement of John R. Fedders, Director, SEC Division of Enforcement); see also *id.* at 28-29, 46, 91, 95, 201, 251-252; H.R. Rep. No. 355, at 27, 29-30.

The Insider Trading Sanctions Act of 1984 proved to be an insufficient deterrent to insider trading. To supplement the ITSA, therefore, Congress passed the Insider Trading and Securities Fraud Enforcement Act of 1988. As Congress declared in its Statement of Findings, "additional methods are appropriate to deter and prosecute violations [of the insider trading laws]." 15 U.S.C. § 78u-1 note. See also H.R. Rep. No. 910, 100th Cong., 2d Sess. 7, 11 (1988).

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[29] See 18 U.S.C. § 3282 (five-year criminal statute of limitations); see also 28 U.S.C. § 2462 (five-year statute of limitations for a "civil fine, penalty or forfeiture").

The ITSFEA affirmed and strengthened the SEC's authority to seek civil penalties up to three times the profit gained or the loss avoided. More importantly for present purposes, Section 20A of the Act also provides a "[p]rivate right[ ] of action based on contemporaneous trading." An insider trader

> shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

15 U.S.C. § 78t-1(a). The Act further provides a "[l]imitation[ ] on liability" based on principles of disgorgement, stating that "[t]he total amount of damages imposed under subsection (a) of this section shall not exceed the profit gained or loss avoided in the transaction or transactions that are the subject of the violation." 15 U.S.C. § 78t-1(b)(1). See also 15 U.S.C. § 78t-1(b)(2) (private remedy to be offset by disgorgement obtained by SEC).

With respect to this express private remedy, the ITSFEA supplies an explicit statute of limitations: "[n]o action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation." 15 U.S.C. § 78t-1(b)(4). The bill introduced in the Senate, as well as that proposed by the SEC, expressly incorporated by reference the limitations provision of the ITSA; the House bill simply reiterated that provision with only technical conforming changes, and the Act was passed in that form. See H.R. 5133, 100th Cong., 2d Sess. § 21A(d)(5) (1988); S. 1380, 100th Cong., 1st Sess. § 16A(f) (1987); *The Insider Trading Proscriptions Act of 1987: Hearing on S. 1380 Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban*

Affairs, 100th Cong., 1st Sess. 30 (1987) (SEC proposed bill).

The SEC contends that it is this five-year limitations provision that should be borrowed for implied 10(b) causes of action. Seizing on the fortuitous enactment of the 1988 statute—a statute that even the SEC does not claim specifically extends beyond insider trading—the SEC's argument represents a result-oriented attempt to find the longest possible federal securities limitations period based on nothing more than the agency's own policy preference. The SEC treats the ITSFEA like a *deus ex machina*, conveniently intervening after half a century to provide a platform for the erection of its argument. This ahistorical approach is an inappropriate method for ascertaining and implementing the policies of Congress. Despite the SEC's contentions, the one-year/three-year provision in the 1933 and 1934 Acts plainly remains the more appropriate statute of limitations to apply.[30]

First, while the express causes of action in the 1933 and 1934 Acts are closely analogous to the 10(b) action (see pages 24-25, *supra*), the private insider trading cause of action in the ITSFEA is quite dissimilar. The insider trading provision is deterrent in nature, not remedial, as its legislative history makes clear. In the same vein, disgorgement relief is entirely a function of the defendant's benefit (either profit gained or loss avoided) from the insider trading, which normally is fixed at or shortly after the time of the violation. By contrast, an out-of-pocket damages remedy may depend on the future market performance of the security—which was one of the principal reasons Congress enacted a short limitations period in the 1933 and 1934 Acts (see pages 32-33, *supra*), but which is irrelevant to disgorgement. See *Short*, 908 F.2d at 1392. Congress's concerns over open-ended liabilities arising long after the date of the alleged violation—concerns greatly intensified by modern class action procedures—apply precisely to implied claims under Section 10(b); it is only because of the limited penalty under the 1988 legislation that a more extended limitations period was thought to be justified.

Second, Congress narrowly restricted the ITSFEA to insider trading and eschewed any intention to affect implied remedies under Section 10(b) and Rule 10b-5. See 15 U.S.C. § 78t-1(d) ("[n]othing in this section shall be construed to limit or condition * * * the availability of any cause of action implied from a provision of this chapter"). This statutory provision is reinforced by its legislative history, which carefully distinguishes the usual private damages remedy for an injured party under the securities laws from the disgorgement provision for contemporaneous traders (whether or not proximately injured by the defendant's violation) under the ITSFEA. See H.R. Rep. No. 910, at 27 ("there clearly are injuries caused by insider trading to others beyond contemporaneous traders," and the legislation "avoid[s] creating an express cause of action which might have the unintended effect of freezing the law or in any way restricting the potential rights of action which have been implied by the courts in this area"); see also *id.* at 28; 134 Cong. Rec. S17218, S17220

[30] The inherent vulnerability of the SEC's position may be seen in the following way. If Congress in the 1934 Act, instead of including a limitations provision in each of the sections creating a cause of action, instead had adopted a single limitations provision applicable to the entire Act—which in fact is the approach that Congress followed in Section 13 of the 1933 Act—there would be no basis for the SEC to argue that the 1988 statute for insider trading suits would have *sub silentio* repealed or amended the 1934 limitations provision. Thus, it is only because of the form of the 1934 Act that the SEC can even advance its argument. Given the strong congressional policies expressed in the one-year/three-year provision and the broad application of that provision across the 1933 and 1934 Acts, it is clear that the basis for the SEC's position is entirely a matter of form and not of substance and provides no reliable guide to the intention of Congress.

(daily ed. Oct. 21, 1988) (statements of Sen. Proxmire and Sen. Garn). Contrary to this clear congressional intent, the SEC's application of the ITSFEA's five-year limitations provision to all 10(b) claims would "limit" or "restrict[ ]" actions that were permissible under existing law prior to 1988.

Third, in contrast to the express limitations provisions in the 1933 and 1934 Acts, the five-year provision in the ITSFEA does not appear to be a statute of repose that absolutely bars suits after the specified time regardless of equitable tolling or estoppel. In its *amicus* brief to this Court in *Lebman* (at 14 n.17), the SEC went to great lengths to argue that the ITSFEA limitation is an absolute statute of repose, and this assertion is an important if not essential premise for the remainder of its submission that this provision should be borrowed in 10(b) suits.

As the court pointed out in *Short*, however, the five-year provision "appears to be an ordinary statute of limitations" rather than a statute of repose; "[t]he language is in the traditional form of a statute of limitations," and the SEC has not "cite[d] any legislative history indicating that it is more potent than the usual variety." 908 F.2d at 1391.

> The difference between statutes of limitations and statutes of repose is substantial in securities litigation. * * * All of the express provisions in the '33 and '34 Acts * * * are drawn as statutes of repose, and deliberately so. * * *
>
> Setting an outer limit for claiming fraud or material omissions in the sale of securities is an important aspect of [the limitations provisions in the 1933 and 1934 Acts, and] one of the principal reasons Congress designed the statute that way.

Id. at 1392. The limited nature of disgorgement relief may explain why Congress was content in the ITSFEA to enact both a longer limitations provision and one that is not

a statute of repose. See *ibid.* ("Section 20A may use a five-year period, and be drafted as an ordinary statute of limitations, precisely because the reasons for setting the shorter one-and-three period for fraud are not present"). But the SEC has offered no reason why Congress would have wanted to depart in implied 10(b) suits from its otherwise consistent pattern in the 1933 and 1934 Acts of adopting short limitations provisions that constitute absolute periods of repose. See ABA Report at 655 ("[a]gainst the clear evidence that Congress affirmatively intended that no tolling doctrine would be available for the express limitations periods for securities actions, it seems implausible that Congress intended such a doctrine to apply to the implied 10b-5 cause of action").

The SEC's brief in *Lebman* advances three grounds for preferring the five-year provision in the ITSFEA, but these do not support its conclusion. The SEC initially takes comfort (*Lebman* Am. Br. 12, 17) from the fact that the ITSFEA is a recent enactment and, as the court phrased the argument in *Short* (908 F.2d at 1391), "represents Congress' latest thoughts." As explained above (see pages 19-20, 27-28, 40, *supra*), however, the recent vintage of the ITSFEA cuts against the SEC's position, for it is the intent and policies behind the 1933 and 1934 Acts that are controlling on the cause of action implied under the 1934 Act. In any event, for the reasons already discussed, the ITSFEA does not in any way undermine or contradict the import of the 1933 and 1934 Acts in this context. Quite simply, in view of the limited scope and focused purpose of the ITSFEA, it "represents Congress' latest thoughts" on a statute that has little if any relationship to ordinary damages litigation under Section 10(b).

Perhaps revealing its true purpose, the SEC also emphasizes (Br. 16) that the five-year provision should be borrowed simply because it is longer than the one-year/three-year provision and thus more favorable to plaintiffs.

But that search for a lengthy limitations period is precisely backwards. Congress deliberately adopted the *shorter* period (and specifically *rejected* a five-year period) in order to further important federal policies under the 1933 and 1934 Acts—policies that, while not appertaining to the limited cause of action in the ITSFEA, are directly relevant to the implied 10(b) cause of action. What is more, Congress did so despite the concern expressed at the time, and repeated now by the SEC, that the one-year/three-year period is too short, especially in light of the scienter requirement in 10(b) suits. See page 33, *supra*. And, as the SEC is forced to admit (Br. 16 n.19), the one-year/three-year limitations provision is expressly applicable to actions under Section 9 of the 1934 Act (15 U.S.C. § 78i), which, like 10(b) actions, require scienter.[31]

Like Congress, this Court too has underscored the problems caused by burdensome and unwarranted securities litigation—problems that would be greatly exacerbated by the longer limitations period the SEC advocates. As the Court has noted, 10(b) suits "present[ ] a danger of vexatiousness different in degree and in kind" from other litigation. *Blue Chip Stamps*, 421 U.S. at 739. "[E]ven a complaint which by objective standards may have very little chance of success at trial has a settlement value to the plaintiff out of any proportion to its prospect of success at trial so long as he may prevent the suit from being resolved against him by dismissal or summary judgement." *Id.* at 740. See also *Blue Shield of Virginia* v. *McCready*, 457 U.S. 465, 477 (1982) ("the potency of the remedy implies the need for some care in its application").

[31] It is significant that state blue sky limitations, which many courts currently apply to 10(b) actions, generally range from one to three years. ABA Report at 650. This is quite in line with the one-year/three-year provision and rebuts the SEC's assertion that such a period is unreasonably short in 10(b) cases. See also *Ceres Partners*, slip op. 35-36.

A plaintiff's ability to extract such an unduly favorable settlement results from a number of considerations: that "[t]he very pendency of the lawsuit may frustrate or delay normal business activity of the defendant which is totally unrelated to the lawsuit" (*Blue Chip Stamps*, 421 U.S. at 740); that there is "the threat of extensive discovery" even in "a lawsuit which is groundless in any event, but cannot be proved so before trial" (*id.* at 742-743); that the "inherent[ ] imprecis[ion]" of 10(b) requirements (*Dirks* v. *SEC*, 463 U.S. 646, 658 n.17 (1983)) and "the indefinite and uncertain disclosure obligations imposed" (*Teamsters* v. *Daniel*, 439 U.S. 551, 569 (1979)) make it all too easy to allege a colorable violation; that a defense against even unmeritorious claims entails "high costs" (*Piper* v. *Chris-Craft Industries*, 430 U.S. 1, 40 (1977)); and that "[c]ertification of a large class," as is common in securities cases, "may so increase the defendant's potential damages liability and litigation costs that he may find it economically prudent to settle and to abandon a meritorious defense." *Coopers & Lybrand* v. *Livesay*, 437 U.S. 463, 476 (1978). Securities trials also involve the special risk of a substantial verdict against a corporate defendant due to jury sympathy for the plaintiff and antipathy for a large (and often out-of-state) company. The statute-of-limitations defense is an important means of weeding out unjustified claims prior to trial and preventing litigious investors from playing a game of "heads I win, tails you lose" with securities defendants. The effectiveness of this defense would be greatly impaired if a five-year limitations period—a period that Congress found too long in the 1933 and 1934 Acts—were applicable.

Finally, the SEC contends (Br. 17) that, because insider trading is one form of 10(b) violation, consistency requires that all 10(b) claims be subject to the insider trading limitations provision in the ITSFEA. This argument cannot be squared with Congress's manifest intent under the se-

curities laws. By its plain terms and unambiguous history, the ITSFEA was limited to the special situation of insider trading. Congress recognized that there was a broad universe of other 10(b) violations, and it could not have stated more clearly that such suits were to be left as they were, unaffected by this narrowly-focused statute. See pages 41-42, *supra*. Beyond this, the divergence between insider trading claims and other 10(b) claims will not cause confusion in practical operation, since a plaintiff under Section 20A will have to "accept the [restrictions] of that statute, including the restriction of damages to the defendants' profit (as opposed to the plaintiff's loss). In the great bulk of cases, there will be no ambiguity." *Short*, 908 F.2d at 1391.

The SEC's proposed solution also would do nothing to cure the perceived problem of inconsistency. While the SEC's approach would result in a single limitations period in 10(b) and ITSFEA insider trading cases, other suits would be subject to different limitations periods for interrelated causes of action. See *Ceres Partners*, slip op. 29-32. For example, it is common for a purchaser-plaintiff to allege fraud by a seller under both Section 12(2) of the 1933 Act (15 U.S.C. § 77*l*(2))—which is governed by the one-year/three-year limitations provision—and Section 10(b)—which the SEC would treat under the five-year limitations provision. Indeed, the SEC acknowledges (Br. 18) that 10(b) actions "now overlap[ ] in significant respects with the coverage of other express causes of action." See generally *Herman & MacLean* v. *Huddleston*, 459 U.S. 375 (1983).[32]

[32] A further anomaly in the SEC's position is that it would "allow many plaintiffs who could have sued on express private causes of action, but whose actions were barred by short limitations periods, to maintain their claims as 10b-5 suits." ABA Report at 647 n.19. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 210 (implied securities remedies should not be construed to "nullify the effectiveness of the carefully drawn procedural restrictions on these express actions").

In the end, the court in *Short* was exactly right in rejecting this contention of the SEC. "Congress did not say that § 20A applies to all cases under Rule 10b-5; it did not amend [the limitations provisions in the 1933 and 1934 Acts]; it limited the scope of § 20A's statute of limitations to a particular and atypical kind of violation." 908 F.2d at 1392. Accordingly, "run-of-the-mine frauds under Rule 10b-5 should be governed by the statute in force when Rule 10b-5 came into being, the statute *designed for* the kind of conduct about which * * * most * * * 10b-5 plaintiffs complain"; to borrow the ITSFEA provision "as the rule for *all* Rule 10b-5 actions, just because a five-year period has been deemed appropriate for one atypical kind of violation, would let the tail wag the dog." *Ibid.* (emphasis in original).[33]

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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[33] Even under the SEC's position—that 10(b) actions are subject to a five-year statute of repose—defendants Comdisco, Inc. and Kenneth N. Pontikes would be entitled to dismissal. The Fourth Amended Complaint concedes (¶ 431) that the 17 Euston Associates plaintiffs (who are the only plaintiffs against these two defendants) made their investments in May and June 1981. Because the earliest complaint of these 17 plaintiffs was filed in November 1986—more than five years after the transactions at issue—their claims plainly are time-barred.

STATUTORY AND REGULATORY APPENDIX

1. Securities Act of 1933, 15 U.S.C. § 77a *et seq.*

A. Section 11, 15 U.S.C. § 77k:

(a) In case any part of the registration statement, when such part became effective, contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary to make the statements therein not misleading, any person acquiring such security (unless it is proved that at the time of such acquisition he knew of such untruth or omission) may, either at law or in equity, in any court of competent jurisdiction, sue—

(1) every person who signed the registration statement;

(2) every person who was a director of (or person performing similar functions) or partner in, the issuer at the time of the filing of the part of the registration statement with respect to which his liability is asserted;

(3) every person who, with his consent, is named in the registration statement as being or about to become a director, person performing similar functions, or partner;

(4) every accountant, engineer, or appraiser, or any person whose profession gives authority to a statement made by him, who has with his consent been named as having prepared or certified any part of the registration statement, or as having prepared or certified any report or valuation which is used in connection with the registration statement, with respect to the statement in such registration statement, report, or valuation, which purports to have been prepared or certified by him;

(5) every underwriter with respect to such security.

If such person acquired the security after the issuer has made generally available to its security holders an earning statement covering a period of at least twelve months beginning after the effective date of the registration statement, then the right of recovery under this subsection shall be conditioned on proof that such person acquired the security relying upon such untrue statement in the registration statement or relying upon the registration statement and not knowing of such omission, but such reliance may be established without proof of the reading of the registration statement by such person.

(b) Notwithstanding the provisions of subsection (a) no person, other than the issuer, shall be liable as provided therein who shall sustain the burden of proof—

(1) that before the effective date of the part of the registration statement with respect to which his liability is asserted (A) he had resigned from or had taken such steps as are permitted by law to resign from, or ceased or refused to act in, every office, capacity, or relationship in which he was described in the registration statement as acting or agreeing to act, and (B) he had advised the Commission and the issuer in writing that he had taken such action and that he would not be responsible for such part of the registration statement; or

(2) that if such part of the registration statement became effective without his knowledge, upon becoming aware of such fact he forthwith acted and advised the Commission, in accordance with paragraph (1), and, in addition, gave reasonable public notice that such part of the registration statement had become effective without his knowledge; or

(3) that (A) as regards any part of the registration statement not purporting to be made on the authority of an expert, and not purporting to be a copy of or extract from a report or valuation of an expert, and not purporting to be made on the authority of a public official document or statement, he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading; and (B) as regards any part of the registration statement purporting to be made upon his authority as an expert or purporting to be a copy of or extract from a report or valuation of himself as an expert, (i) he had, after reasonable investigation, reasonable ground to believe and did believe, at the time such part of the registration statement became effective, that the statements therein were true and that there was no omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or (ii) such part of the registration statement did not fairly represent his statement as an expert or was not a fair copy of or extract from his report or valuation as an expert; and (C) as regards any part of the registration statement purporting to be made on the authority of an expert (other than himself) or purporting to be a copy of or extract from a report or valuation of an expert (other than himself), he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue or that there

was an omission to state a material fact required to be stated therein or necessary to make the statements therein not misleading, or that such part of the registration statement did not fairly represent the statement of the expert or was not a fair copy of or extract from the report or valuation of the expert; and (D) as regards any part of the registration statement purporting to be a statement made by an official person or purporting to be a copy of or extract from a public official document, he had no reasonable ground to believe and did not believe, at the time such part of the registration statement became effective, that the statements therein were untrue, or that there was an omission to state a material fact required to be stated therein or necessary to make the statement therein not misleading, or that such part of the registration statement did not fairly represent the statement made by the official person or was not a fair copy of or extract from the public official document.

(c) In determining, for the purpose of paragraph (3) of subsection (b) of this section, what constitutes reasonable investigation and reasonable ground for belief, the standard of reasonableness shall be that required of a prudent man in the management of his own property.

(d) If any person becomes an underwriter with respect to the security after the part of the registration statement with respect to which his liability is asserted has become effective, then for the purposes of paragraph (3) of subsection (b) of this section such part of the registration statement shall be considered as having become effective with respect to such person as of the time when he became an underwriter.

(e) The suit authorized under subsection (a) may be to recover such damages as shall represent the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and (1) the value thereof as of the time such suit was brought, or (2) the price at which such security shall have been disposed of in the market before suit, or (3) the price at which such security shall have been disposed of after suit but before judgment if such damages shall be less than the damages representing the difference between the amount paid for the security (not exceeding the price at which the security was offered to the public) and the value thereof as of the time such suit was brought: Provided, that if the defendant proves that any portion or all of such damages represents other than the depreciation in value of such security resulting from such part of the registration statement, with respect to which his liability is asserted, not being true or omitting to state a material fact required to be stated therein or necessary to make the statements therein not misleading, such portion of or all such damages shall not be recoverable. In no event shall any underwriter (unless such underwriter shall have knowingly received from the issuer for acting as an underwriter some benefit, directly or indirectly, in which all other underwriters similarly situated did not share in proportion to their respective interests in the underwriting) be liable in any suit or as a consequence of suits authorized under subsection (a) for damages in excess of the total price at which the securities underwritten by him and distributed to the public were offered to the public. In any suit under this or any other section of this title the court may, in its discretion, require an undertaking for the payment of the costs of such suit, including reasonable attorney's fees, and if judgment shall be rendered against a party litigant, upon the

motion of the other party litigant, such costs may be assessed in favor of such party litigant (whether or not such undertaking has been required) if the court believes the suit or the defense to have been without merit, in an amount sufficient to reimburse him for the reasonable expenses incurred by him, in connection with such suit, such costs to be taxed in the manner usually provided for taxing of costs in the court in which the suit was heard.

(f) All or any one or more of the persons specified in subsection (a) shall be jointly and severally liable, and every person who becomes liable to make any payment under this section may recover contribution as in cases of contract from any person who, if sued separately, would have been liable to make the same payment, unless the person who has become liable was, and the other was not, guilty of fraudulent misrepresentation.

(g) In no case shall the amount recoverable under this section exceed the price at which the security was offered to the public.

B. Section 12, 15 U.S.C. § 77*l*:

Any person who

(1) offers or sells a security in violation of section 5, or

(2) offers or sells a security (whether or not exempted by the provisions of section 3, other than paragraph (2) of subsection (a) thereof), by the use of any means or instruments of transportation or communication in interstate commerce or of the mails, by means of a prospectus or oral communication, which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of

the circumstances under which they were made, not misleading (the purchaser not knowing of such untruth or omission), and who shall not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of such untruth or omission,

shall be liable to the person purchasing such security from him, who may sue either at law or in equity in any court of competent jurisdiction, to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security.

C. Section 13, 15 U.S.C. § 77m:

No action shall be maintained to enforce any liability created under section 11 or section 12(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 12(1), unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 11 or section 12(1) more than three years after the security was bona fide offered to the public, or under section 12(2) more than three years after the sale.

2. Securities Exchange Act of 1934, 15 U.S.C. § 78a *et seq*.

A. Section 9, 15 U.S.C. § 78i:

(a) It shall be unlawful for any person, directly or indirectly, by the use of the mails or any means or instrumentality of interstate commerce, or of

any facility of any national securities exchange, or for any member of a national securities exchange—

(1) For the purpose of creating a false or misleading appearance of active trading in any security registered on a national securities exchange, or a false or misleading appearance with respect to the market for any such security, (A) to effect any transaction in such security which involves no change in the beneficial ownership thereof, or (B) to enter an order or orders for the purchase of such security with the knowledge that an order or orders of substantially the same size, at substantially the same time and at substantially the same price, for the sale of any such security, has been or will be entered by or for the same or different parties, or (C) to enter any order or orders for the sale of any such security with the knowledge that an order or orders of substantially the same size, at substantially the same time, and at substantially the same price, for the purchase of such security, has been or will be entered by or for the same or different parties.

(2) To effect, alone or with one or more other persons, a series of transactions in any security registered on a national securities exchange creating actual or apparent active trading in such security or raising or depressing the price of such security, for the purpose of inducing the purchase or sale of such security by others.

(3) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination in the ordinary

course of business of information to the effect that the price of any such security will or is likely to rise or fall because of market operations of any one or more persons conducted for the purpose of raising or depressing the prices of such security.

(4) If a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to make, regarding any security registered on a national securities exchange, for the purpose of inducing the purchase or sale of such security, any statement which was at the time and in the light of the circumstances under which it was made, false or misleading with respect to any material fact, and which he knew or had reasonable ground to believe was so false or misleading.

(5) For a consideration, received directly or indirectly from a dealer or broker, or other person selling or offering for sale or purchasing or offering to purchase the security, to induce the purchase or sale of any security registered on a national securities exchange by the circulation or dissemination of information to the effect that the price of any such security will or is likely to rise or fall because of the market operations of any one or more persons conducted for the purpose of raising or depressing the price of such security.

(6) To effect either alone or with one or more other persons any series of transactions for the purchase and/or sale of any security registered on a national securities exchange for the purpose of pegging, fixing, or stabilizing the price of such security in contravention of such rules and regulations as the Commission may prescribe as necessary or appro-

priate in the public interest or for the protection of investors.

(b) It shall be unlawful for any person to effect, by use of any facility of a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors—

(1) any transaction in connection with any security whereby any party to such transaction acquires any put, call, straddle, or other option or privilege of buying the security from or selling the security to another without being bound to do so; or

(2) any transaction in connection with any security with relation to which he has, directly or indirectly, any interest in any such put, call, straddle, option, or privilege; or

(3) any transaction in any security for the account of any person who he has reason to believe has, and who actually has, directly or indirectly, any interest in any such put, call straddle, option, or privilege with relation to such security.

(c) It shall be unlawful for any member of a national securities exchange directly or indirectly to endorse or guarantee the performance of any put, call, straddle, option, or privilege in relation to any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(d) The terms "put", "call", "straddle", "option", or "privilege" as used in this section shall not include any registered warrant, right, or convertible security.

(e) Any person who willfully participates in any act or transaction in violation of subsection (a), (b), or (c) of this section, shall be liable to any person who shall purchase or sell any security at a price which was affected by such act or transaction, and the person so injured may sue in law or in equity in any court of competent jurisdiction to recover the damages sustained as a result of any such act or transaction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant. Every person who becomes liable to make any payment under this subsection may recover contribution as in cases of contract from any person who, if joined in the original suit, would have been liable to make the same payment. No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

(f) The provisions of subsection (a) shall not apply to an exempted security.

(g) Notwithstanding any other provision of law, the Commission shall have the authority to regulate the trading of any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency (but not, with respect to any of the foregoing, an option on a contract for future delivery).

B. Section 10, 15 U.S.C. § 78j:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumen-

tality of interstate commerce or of the mails, or of any facility of any national securities exchange—

(a) To effect a short sale, or to use or employ any stop-loss order in connection with the purchase or sale, of any security registered on a national securities exchange, in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

C. Section 16, 15 U.S.C. § 78p:

(a) Every person who is directly or indirectly the beneficial owner of more than 10 per centum of any class of any equity security (other than an exempted security) which is registered pursuant to section 12 of this title, or who is a director or an officer of the issuer of such security, shall file, at the time of the registration of such security on a national securities exchange or by the effective date of a registration statement filed pursuant to section 12(g) of this title, or within ten days after he becomes such beneficial owner, director, or officer, a statement with the Commission (and, if such security is registered on a national securities exchange, also with the exchange) of the amount of all equity securities of such issuer of which he is the beneficial owner, and within ten days after the close of each calendar month thereafter, if

there has been a change in such ownership during such month, shall file with the Commission (and if such security is registered on a national securities exchange, shall also file with the exchange) a statement indicating his ownership at the close of the calendar month and such changes in his ownership as have occurred during such calendar month.

(b) For the purpose of preventing the unfair use of information which may have been obtained by such beneficial owner, director, or officer by reason of his relationship to the issuer, any profit realized by him from any purchase and sale, or any sale and purchase, of any equity security of such issuer (other than an exempted security) within any period of less than six months, unless such security was acquired in good faith in connection with a debt previously contracted, shall inure to and be recoverable by the issuer, irrespective of any intention on the part of such beneficial owner, director, or officer in entering into such transaction of holding the security purchased or of not repurchasing the security sold for a period exceeding six months. Suit to recover such profit may be instituted at law or in equity in any court of competent jurisdiction by the issuer, or by the owner of any security of the issuer in the name and in behalf of the issuer if the issuer shall fail or refuse to bring such suit within sixty days after request or shall fail diligently to prosecute the same thereafter; but no such suit shall be brought more than two years after the date such profit was realized. This subsection shall not be construed to cover any transaction where such beneficial owner was not such both at the time of the purchase and sale, or the sale and purchase, of the security involved, or any transaction or transactions which the Commission by rules and regulations may exempt as not comprehended within the purpose of this subsection.

(c) It shall be unlawful for any such beneficial owner, director, or officer, directly or indirectly, to sell any equity security of such issuer (other than an exempted security), if the person selling the security or his principal (1) does not own the security sold, or (2) if owning the security, does not deliver it against such sale within twenty days thereafter, or does not within five days after such sale deposit it in the mails or other usual channels of transportation; but no person shall be deemed to have violated this subsection if he proves that notwithstanding the exercise of good faith he was unable to make such delivery or deposit within such time, or that to do so would cause undue inconvenience or expense.

(d) The provisions of subsection (b) of this section shall not apply to any purchase and sale, or sale and purchase, and the provisions of subsection (c) of this section shall not apply to any sale, of an equity security not then or theretofore held by him in an investment account, by a dealer in the ordinary course of his business and incident to the establishment or maintenance by him of a primary or secondary market (otherwise than on a national securities exchange or an exchange exempted from registration under section 5 of this title) for such security. The Commission may, by such rules and regulations as it deems necessary or appropriate in the public interest, define and prescribe terms and conditions with respect to securities held in an investment account and transactions made in the ordinary course of business and incident to the establishment or maintenance of a primary or secondary market.

(e) The provisions of this section shall not apply to foreign or domestic arbitrage transactions unless made in contravention of such rules and regulations as the Commission may adopt in order to carry out the purposes of this section.'

D. Section 18, 15 U.S.C. § 78r:

(a) Any person who shall make or cause to be made any statement in any application, report, or document filed pursuant to this title or any rule or regulation thereunder or any undertaking contained in a registration statement as provided in subsection (d) of section 15 of this title, which statement was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact, shall be liable to any person (not knowing that such statement was false or misleading) who, in reliance upon such statement, shall have purchased or sold a security at a price which was affected by such statement, for damages caused by such reliance, unless the person sued shall prove that he acted in good faith and had no knowledge that such statement was false or misleading. A person seeking to enforce such liability may sue at law or in equity in any court of competent jurisdiction. In any such suit the court may, in its discretion, require an undertaking for the payment of the costs of such suit, and assess reasonable costs, including reasonable attorneys' fees, against either party litigant.

(b) Every person who becomes liable to make payment under this section may recover contribution as in cases of contact from any person who, if joined in the original suit, would have been liable to make the same payment.

(c) No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued.

E. Section 29, 15 U.S.C. § 78cc:

(a) Any condition, stipulation, or provision binding any person to waive compliance with any pro-

vision of this title or of any rule or regulation thereunder, or of any rule of an exchange required thereby shall be void.

(b) Every contract made in violation of any provision of this title or of any rule or regulation thereunder, and every contract (including any contract for listing a security on an exchange) heretofore or hereafter made the performance of which involves the violation of, or the continuance of any relationship or practice in violation of, any provision of this title or any rule or regulation thereunder, shall be void (1) as regards the rights of any person who, in violation of any such provision, rule, or regulation, shall have made or engaged in the performance of any such contract, and (2) as regards the rights of any person who, not being a party to such contract, shall have acquired any right thereunder with actual knowledge of the facts by reason of which the making or performance of such contract was in violation of any such provision, rule, or regulation: *Provided,* (A) That no contract shall be void by reason of this subsection because of any violation of any rule or regulation prescribed pursuant to paragraph (2) or (3) of subsection (c) of section 15 of this title, and (B) that no contract shall be deemed to be void by reason of this subsection in any action maintained in reliance upon this subsection, by any person to or for whom any broker or dealer sells, or from or for whom any broker or dealer purchases, a security in violation of any rule or regulation prescribed pursuant to paragraph (1) of subsection (c) of section 15 of this title, unless such action is brought within one year after the discovery that such sale or purchase involves such violation and within three years after such violation.

(c) Nothing in this title shall be construed (1) to affect the validity of any loan or extension of credit (or any extension or renewal thereof) made

or of any lien created prior or subsequent to the enactment of this title, unless at the time of the making of such loan or extension of credit (or extension or renewal thereof) or the creating of such lien, the person making such loan or extension of credit (or extension or renewal thereof) or acquiring such lien shall have actual knowledge of facts by reason of which the making of such loan or extension of credit (or extension or renewal thereof) or the acquisition of such lien is a violation of the provisions of this title or any rule or regulation thereunder, or (2) to afford a defense to the collection of any debt or obligation or the enforcement of any lien by any person who shall have acquired such debt, obligation, or lien in good faith for value and without actual knowledge of the violation of any provision of this title or any rule or regulation thereunder affecting the legality of such debt, obligation, or lien.

3. Insider Trading Sanctions Act of 1984, adding Section 21(d)(2) of the Securities Exchange Act of 1934, 15 U.S.C. § 78u(d)(2) (Supp. IV 1986), as amended and recodified, Section 21A of the Securities Exchange Act of 1934, 15 U.S.C. § 78u-1 (1988):

(a) Authority to impose civil penalties

(1) Judicial actions by Commission authorized

Whenever it shall appear to the Commission that any person has violated any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information in, or has violated any such provision by communicating such information in connection with, a transaction on or through the facilities of a national securities exchange or from or through a broker or dealer, and which is not part of a public offering by an issuer of securities other than standardized options, the Commission—

(A) may bring an action in a United States district court to seek, and the court shall have jurisdiction to impose, a civil penalty to be paid by the person who committed such violation; and

(B) may, subject to subsection (b)(1) of this section, bring an action in a United States district court to seek, and the court shall have jurisdiction to impose, a civil penalty to be paid by a person who, at the time of the violation, directly or indirectly controlled the person who committed such violation.

(2) Amount of penalty for person who committed violation

The amount of the penalty which may be imposed on the person who committed such violation shall be determined by the court in light of the facts and circumstances, but shall not exceed three times the profit gained or loss avoided as a result of such unlawful purchase, sale, or communication.

(3) Amount of penalty for controlling person

The amount of the penalty which may be imposed on any person who, at the time of the violation, directly or indirectly controlled the person who committed such violation, shall be determined by the court in light of the facts and circumstances, but shall not exceed the greater of $1,000,000, or three times the amount of the profit gained or loss avoided as a result of such controlled person's violation. If such controlled person's violation was a violation by communication, the profit gained or loss avoided as a result of the violation shall, for purposes of this paragraph only, be deemed to be limited to the profit gained or loss avoided by the person or persons to whom the controlled person directed such communication.

(b) Limitations on liability

(1) Liability of controlling persons

No controlling person shall be subject to a penalty under subsection (a)(1)(B) of this section unless the Commission establishes that—

(A) such controlling person knew or recklessly disregarded the fact that such controlled person was likely to engage in the act or acts constituting the violation and failed to take appropriate steps to prevent such act or acts before they occurred; or

(B) such controlling person knowingly or recklessly failed to establish, maintain, or enforce any policy or procedure required under section 78*o*(f) of this title or section 80b-4a of this title and such failure substantially contributed to or permitted the occurrence of the act or acts constituting the violation.

(2) Additional restrictions on liability

No person shall be subject to a penalty under subsection (a) of this section solely by reason of employing another person who is subject to a penalty under such subsection, unless such employing person is liable as a controlling person under paragraph (1) of this subsection. Section 78t(a) of this title shall not apply to actions under subsection (a) of this section.

(c) Authority of Commission

The Commission, by such rules, regulations, and orders as it considers necessary or appropriate in the public interest or for the protection of investors, may exempt, in whole or in part, either unconditionally or upon specific terms and conditions, any person or transaction or class of persons or transactions from this section.

(d) Procedures for collection

(1) Payment of penalty to Treasury

A penalty imposed under this section shall (subject to subsection (e) of this Section) be payable into the Treasury of the United States.

(2) Collection of penalties

If a person upon whom such a penalty is imposed shall fail to pay such penalty within the time prescribed in the court's order, the Commission may refer the matter to the Attorney General who shall recover such penalty by action in the appropriate United States district court.

(3) Remedy not exclusive

The actions authorized by this section may be brought in addition to any other actions that the Commission or the Attorney General are entitled to bring.

(4) Jurisdiction and venue

For purposes of section 78aa of this title, actions under this section shall be actions to enforce a liability or a duty created by this chapter.

(5) Statute of limitations

No action may be brought under this section more than 5 years after the date of the purchase or sale. This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this chapter, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties, imposed in an action commenced within 5 years of such transaction.

(e) Authority to award bounties to informants

Notwithstanding the provisions of subsection (d)(1) of this Section, there shall be paid from amounts im-

posed as a penalty under this section and recovered by the Commission or the Attorney General, such sums, not to exceed 10 percent of such amounts, as the Commission deems appropriate, to the person or persons who provide information leading to the imposition of such penalty. Any determinations under this subsection, including whether, to whom, or in what amount to make payments, shall be in the sole discretion of the Commission, except that no such payment shall be made to any member, officer, or employee of any appropriate regulatory agency, the Department of Justice, or a self-regulatory organization. Any such determination shall be final and not subject to judicial review.

(f) Definition

For purposes of this section, "profit gained" or "loss avoided" is the difference between the purchase or sale price of the security and the value of that security as measured by the trading price of the security a reasonable period after public dissemination of the nonpublic information.

4. Insider Trading and Securities Fraud Enforcement Act of 1988, adding Section 20A of the Securities Exchange Act of 1934, 15 U.S.C. § 78t-1:

(a) Private rights of action based on contemporaneous trading

Any person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

(b) Limitations on liability

(1) Contemporaneous trading actions limited to profit gained or loss avoided

The total amount of damages imposed under subsection (a) shall not exceed the profit gained or loss avoided in the transaction or transactions that are the subject of the violation.

(2) Offsetting disgorgements against liability

The total amount of damages imposed against any person under subsection (a) shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 78u(d) of this title relating to the same transaction or transactions.

(3) Controlling person liability

No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under this section shall be subject to section 78t(a) of this title.

(4) Statute of limitations

No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

(c) Joint and several liability for communicating

Any person who violates any provision of this title or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) of this Section with, and to the same extent as, any person or persons liable under subsection (a) to whom the communication was directed.

(d) Authority not to restrict other express or implied rights of action

Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this chapter or the availability of any cause of action implied from a provision of this chapter.

(e) Provisions not to affect public prosecutions

This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this chapter, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties.

5. SEC Rule 10b-5, 17 C.F.R. § 240.10b-5:

Employment of Manipulative and Deceptive Devices. It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

(12)

No. 90-353

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CLERK

In The

Supreme Court of the United States

October Term, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,

Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ and ANTHONY E. CATALAN, *et al.*,

Respondents.

On Writ Of Certiorari
To The United States Court of Appeals
For The Ninth Circuit

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QUESTIONS PRESENTED

1. Should the statute of limitations for private actions under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5, promulgated thereunder, 17 C.F.R. § 240.10b-5, be determined by state common law fraud statutes of limitations which are discovery-based and do not have unduly short statutes of repose or by a federal statute such as the Interstate Land Sales Full Disclosure Act, the Insider Trading Act or one of the various express remedies in the Securities Act of 1933 or the Securities Exchange Act of 1934?

2. If a new, uniform statute of limitations is adopted, should it be subject to the doctrines of equitable tolling and fraudulent concealment?

3. Should a new statute of limitations be applied retroactively?

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No. 90-333

In The

Supreme Court of the United States

October Term, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,

Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ and ANTHONY E. CATALAN, *et al.*,

Respondents.

On Writ Of Certiorari
To The United States Court of Appeals
For The Ninth Circuit

BRIEF FOR RESPONDENTS

STATUTES

This case involves the statutes, regulations, and rules set forth by Petitioner and the following additional statutes which are set forth verbatim in the Appendix to this Brief.

1. Sections 1404(a), 1410(a)-(b), and 1412(a) of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. §§ 1703(a), 1709(a)-(b), 1711(a).

2. Section 313 of the Judicial Improvements Act of 1990, Pub. L. No. 101-650, 104 Stat. 5115.

STATEMENT OF THE CASE

Respondents correct and supplement Petitioner's statement in certain respects.

The sole issue decided by the trial court on summary judgment was whether plaintiffs were on inquiry notice of fraud more than two years before commencing their § 10(b) claims and more than four years before commencing their RICO claims.[1] This issue involved applying federal law to the facts of the case. While the applicable statute of limitations for the § 10(b) claims was determined by state law, when the statute of limitations began to run was a question of federal law. *See* Pet.'s Cert. Br. at 12A-13A.

For purposes of summary judgment, the parties and the trial court accepted plaintiffs' allegations as true. Plaintiffs alleged that the offering memoranda represented the limited partnerships would own valuable computer hardware and software. JA 17-18. In fact, several of the partnerships never owned any hardware. JA 68, 85, 102, 220. Other partnerships owned hardware that was knowingly overvalued, and all of the software was knowingly overvalued.[2] Petitioner and the other defendants knowingly or recklessly participated in the fraud. *See e.g.*, JA 41 (*Reitz* Fourth Amended Complaint, ¶¶ 54 and 55). Contrary to Petitioner's statement, there is no evidence that Petitioner merely prepared a model offering

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[1] This case involves the consolidated actions of *John V. Reitz, et al. v. Leasing Consultants, et al.*, Ninth Circuit Case No. 88-4077, *John Gilbertson, et al. v. Anders G. Arnheim, et al.*, Ninth Circuit Case No. 88-4100, and *Anthony E. Catalan v. Paulson Investment Company, Inc., et al.*, Ninth Circuit Case No. 88-4099, which will herein be referred to as "*Reitz*", "*Gilbertson*" and "*Catalan*".

[2] There are seven separate limited partnerships. For examples of allegations of overvaluation common to each limited partnership, *see* JA 28, 29, 31-32, 33, 36, 37 and 38 (*Reitz* Fourth Amended Complaint, ¶¶ 34(b), (c), (e) and (f), 38(g) and (h), 39(b) and (c), and 40(a) and (c), relating to the Duval Limited Partnership).

memorandum. In six of the seven limited partnerships, Petitioner prepared the offering memoranda in question, was general or tax counsel, wrote tax opinions which contained key misrepresentations and which were used in the offering memoranda, and wrote model partnership and lease agreements. Lampf further assisted in concealing the fraud. JA 33-39, 40, 49-56, 65-70, 72-73, 82-89, 98-104, 106, 115-120, 122.

Plaintiffs are residents of Oregon, California and Washington. Defendants knew the investments would be sold in Oregon. They did not argue in the lower courts that the applicable statute of limitations for the § 10(b) claims should be found elsewhere than in Oregon common law fraud, unless the court was going to overrule prior case law and apply a federal statute of limitations.

The "periodic written reports" (the Lawrence Reports) were written to allay any suspicion of fraud. JA 39, 54-55, 71, 88-89, 105, 121 and 223. The promoters, who had knowingly created the fraudulent investments, installed a purported expert in computer matters to write the reports to give an explanation for the lack of financial success of the investments. *Id.* In the case of one partnership, they also restructured the investment to purchase real estate to replace the software. JA 71-72. In the case of the other partnerships, they installed one of their cohorts (unbeknownst to plaintiffs) as the general partner or administrative assistant. This further allayed any suspicion of fraud. As the Ninth Circuit explained:

> . . . Appellants' knowledge that the software investment had performed dramatically below projections did not necessarily suggest intentional misrepresentation of income projections, upon which the software appraisals were based, at offering time. Rather, the software failures could have resulted from realization of the risks of technological obsolescence, market change, and lessee marketing difficulties – of which the offering memoranda had warned and to which the Lawrence Reports (except possibly those sent to the Euston Associates investors) had ascribed the failures.

Pet.'s Cert. Br. at 14A.

Plaintiffs did not discover the fraudulent nature of the investments until an attorney hired by one of the general partners to defend Internal Revenue Service audits discovered there simply was no hardware for some of the partnerships. JA 40, 55, 72, 89, 106, 122 and 224.

This case should be affirmed and remanded if this Court continues to apply the Oregon common law fraud statute of limitations or a similar statute of limitations that does not have a three year statute of repose. Also, the case should be remanded if a new statute of limitations that bars plaintiffs' claims on its face is not applied retroactively or if the doctrines of fraudulent concealment or equitable tolling apply.

SUMMARY OF ARGUMENT

The issue before this Court is whether the statute of limitations for § 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder, 17 C.F.R. § 240.10b-5, (referred to collectively as "§ 10(b)") should be drawn from state or federal law. Applying the traditional rule of borrowing state law where no express statute of limitations exists for a federal cause of action, courts have, until recently, uniformly looked to analogous state law.[3] The exceptions to the traditional rule do

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[3] Prior to *In re Data Access Sys. Sec. Litig.*, 843 F.2d 1537 (3d Cir.) (*en banc*), *cert. denied*, 488 U.S. 849 (1988), all twelve circuits borrowed the forum state's statutes of limitations. *See, e.g., Corwin v. Marney, Orton Inv.*, 843 F.2d 194 (5th Cir.), *cert. denied*, 488 U.S. 924 (1988); *Suslick v. Rothschild Sec. Corp.*, 741 F.2d 1000 (7th Cir. 1984); *Vucinich v. Paine, Webber, Jackson & Curtis, Inc.*, 739 F.2d 1434 (9th Cir. 1984); *Kennedy v. Tallant*, 710 F.2d 711 (11th Cir. 1983); *Armstrong v. McAlpin*, 699 F.2d 79 (2d Cir. 1983); *Herm v. Stafford*, 663 F.2d 669 (6th Cir. 1981); *Sharp v. Coopers & Lybrand*, 649 F.2d 175 (3d Cir. 1981), *cert. denied*, 455 U.S. 938 (1982); *Buder v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 644 F.2d 690 (8th Cir. 1981); *O'Hara v. Kovens*, 625 F.2d

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not apply here. State common law fraud law remains the most analogous body of law. It has a discovery-based statute of limitations and does not have a short three year statute of repose. It best accommodates the policies furthered by § 10(b) and the practicalities of § 10(b) fraud litigation.

Petitioner argues that this Court should apply the one year from discovery/three year from sale ("one year/three year") limitation and repose period of the express, private remedies provided in the Securities Act of 1933 and the Securities Exchange Act of 1934 (referred to collectively as the "Acts"). The substance of Petitioner's argument is that had the 73rd Congress enacted an express right of action for § 10(b), it would have applied a one year/three year limitation period as it had done for the express private remedies.

Neither Congress nor the Commission ever considered the possibility of there existing a private right of action under § 10(b) and Rule 10b-5. *See Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730, 737 (1975) (emphasizing there is no legislative intent concerning private actions under Rule 10b-5, as it is a "judicial oak which has grown from little more than a legislative acorn"). Where no limitations period is expressly provided for in a federal cause of action, this

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15 (4th Cir. 1980), *cert. denied*, 449 U.S. 1124 (1981); *Wachovia Bank & Trust Co. v. Nat'l Student Mktg. Corp.*, 650 F.2d 342 (D.C. Cir. 1980), *cert. denied*, 452 U.S. 954 (1981); *Cook v. Avien, Inc.*, 573 F.2d 685 (1st Cir. 1978); *de Haas v. Empire Petro. Co.*, 435 F.2d 1223 (10th Cir. 1970).

Even after *Data Access*, most courts that have considered *Data Access* have declined to abandon the traditional rule of borrowing state law. *E.g., Bath v. Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817 (10th Cir. 1990); *Nesbit v. McNeil*, 896 F.2d 380 (9th Cir. 1990); *Smith v. Duff & Phelps, Inc.*, 891 F.2d 1567 (11th Cir. 1990); *Roney & Co. v. Goren*, 875 F.2d 1218 (6th Cir. 1989); *Mercer v. Jaffe, Snider, Raitt & Hever, P.C.*, 713 F.Supp. 1019 (W.D. Mich. 1989); *Corwin v. Marney, supra; Durham v. Business Management Assocs.*, 847 F.2d 1505 (11th Cir. 1988); *Ebrahimi v. E.F. Hutton & Co., Inc.*, 852 F.2d 516 (10th Cir. 1988); *TCF Banking & Savings, F.A. v. Arthur Young & Co.*, 697 F.Supp. 362 (D. Minn. 1988).

Court has consistently applied the analysis outlined in *DelCostello v. International Bd. of Teamsters*, 462 U.S. 151 (1983). Under this analysis, "analogous state statutes of limitations are to be used unless they frustrate or significantly interfere with federal policies" and the practicalities of litigation, *Reed v. United Transport. Union*, 488 U.S. 319, 327 (1989), *and* "federal law clearly provides a closer analogy" than state law, *DelCostello*, 462 U.S. at 172. Congress intends by its silence that courts should apply state law. *Agency Holding Corp. v. Malley-Duff & Assocs.*, 483 U.S. 143, 147 (1987). Legislative intent may be relevant to the federal policies at stake but not to guess what Congress might have provided in a statute of limitations, particularly where legislative intent is of little assistance even in "divining" the contours of a § 10(b) cause of action. *Blue Chip Stamps*, 421 U.S. at 737.

The fundamental purpose behind the federal securities laws is to protect the investor by: (1) insuring full disclosure and (2) preventing fraud. *See Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 195 (1976). In the express remedies, Congress eliminated or relaxed the requirements of proving scienter, reliance, and causation and shifted the burden of proof to defendants to assure full disclosure and protect investors. Scrutiny of the national exchanges by the public, the media and the SEC and the lack of a scienter requirement ensure that violations of the express remedies do not go long unnoticed. In light of the relatively light burden placed upon a plaintiff and the relative ease of early detection of wrongdoing, the one year/three year limitations period is suited for the express remedies.

In contrast, a § 10(b) action is a fraud based claim. It not only requires proof of misstatement, nondisclosure or manipulation, but also proof of scienter, reliance and causation. *Ernst & Ernst*, 425 U.S. at 193. The elements of a common law fraud claim are substantially similar to the elements of a § 10(b) claim. Thus, common law fraud is sufficiently analogous for statute of limitations purposes. This Court has interpreted § 10(b) in view of the differences between § 10(b) and the express remedies, including the different statute of limitations periods. *Id.* at 210, n.29; *Herman & MacLean v. Huddleston*, 459 U.S. 375, 384 n.18 (1983).

The relatively longer, discovery-based limitation periods for common law fraud and the absence of a short repose period further

the remedial purposes of the Acts and the policy of encouraging private litigation of the federal securities laws. It accommodates the practicalities of § 10(b) litigation where fraud, in many instances, simply cannot be discovered in three years. Applying the approach used in *Wilson v. Garcia*, 471 U.S. 261 (1985), characterizing all § 10(b) claims as actions for fraud sufficiently accommodates interests in uniformity and certainty.

The express remedies, on the other hand, are not as analogous to § 10(b) as is common law fraud. The three year period of repose would frustrate the policies furthered by § 10(b) and ignore the practicalities of litigation. Section 10(b) has become a catchall provision for all types of fraud to which the express remedies do not apply, such as churning and suitability claims against brokers, market manipulation, fraud involving limited partnerships, fraud in national markets and liability on the part of aiders and abettors. A three year period of repose would foreclose many claims even before an investor should have reasonably discovered fraud. It would remove the key federal remedy in all cases where fraud goes undetected for three years. For example, in Ponzi schemes, cases with a series of fraudulent audited financial statements, bond cases, and limited partnerships, an investor can be easily led to believe for more than three years that the investment is not fraudulent. A three year period of repose would simply prevent many plaintiffs from obtaining any relief under the federal securities laws. It would undermine the remedial purpose of the Acts and the policy of encouraging private litigation. It would institute a policy of *caveat emptor* that is inconsistent with the policies of the securities laws. Moreover, where promoters and their assistants are able to hide fraud for more than three years, plaintiffs will be forced to find relief under state law and will file their claims in a multitude of state and federal courts.

Petitioner's argument is weakened by Congress' acquiescence, for the past 45 years, in the borrowing of state law for § 10(b) claims and Congress' most recent treatment of fraud. In § 20A of the Insider Trading & Securities Fraud Enforcement Act of 1988 ("Insider Trading Act"), 15 U.S.C. § 78t-1, Congress provided a limitations period of five years from the date of the last transaction, 15 U.S.C. § 78t-1(b)(4), for insider trading, a particular type of Rule 10b-5 violation. In the Interstate Land Sales Full Disclosure

Act ("Interstate Land Sales Act"), 15 U.S.C. § 1701 *et seq.*, Congress provided a private cause of action virtually identical to Rule 10b-5 and for the same remedial purpose of combatting fraud. Unlike the one year/three year limitations period of the express actions, the Interstate Land Sales Act allows actions for fraud to be brought within three years from discovery and is not subject to a short period of repose. 15 U.S.C. § 1711(a)(2).

Should this Court decide to abandon the traditional borrowing rule and look to federal law, the limitation periods provided in the Interstate Land Sales Act and § 20A of the Insider Trading Act are more suitable to § 10(b) actions than the three year period of repose of the express remedies. Further, the Court may wish to consider § 313 of the recently enacted Judicial Improvements Act of 1990, Pub. L. No. 101-650, 104 Stat. 5115. While prospective only, it also provides an alternative solution. It provides for a uniform statute of limitations of four years from accrual for all causes of action not subject to an express limitations period.

Finally, if a new limitations period is adopted, it should be subject to the doctrines of equitable tolling and fraudulent concealment, and should not be applied retroactively.

ARGUMENT

I. THE TRADITIONAL RULE IS TO BORROW STATE STATUTES OF LIMITATIONS *UNLESS* FEDERAL LAW IS CLEARLY MORE ANALOGOUS, AND THE APPLICATION OF STATE LAW CONFLICTS WITH FEDERAL POLICIES AND PRACTICALITIES OF LITIGATION.

Section 10(b) does not expressly provide for a private cause of action and, consequently, has no express statute of limitations. In such instances, the traditional rule is to apply the most analogous statute of limitations of the forum state. "As early as 1830, this Court held that state statutes of limitations govern the timeliness of federal causes of action

unless Congress has specifically provided otherwise." *Auto Workers v. Hoosier Cardinal Corp.*, 383 U.S. 696, 703-4 (1966).[4] In *Reed*, this Court recently reiterated that it "generally conclude[s] that Congress intended that the courts apply the most closely analogous statute of limitations under state law." 488 U.S. at 323 (quoting *DelCostello*, 462 U.S. at 158). "Given our longstanding practice of borrowing state law, and the congressional awareness of this practice, we can generally assume that Congress intends by its silence that we borrow state law."[5] *Agency Holding Corp. v. Malley-Duff & Assocs., Inc.*, 483 U.S. 143, 147 (1987).

In rare instances, "state statutes of limitations can be unsatisfactory vehicles for the enforcement of federal law. In those instances, it may be inappropriate to conclude that Congress would choose to adopt state rules at odds with the purpose or operation of federal substantive law." *DelCostello*, 462 U.S. at 161. Courts should forsake the traditional rule of

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[4] *Accord McCluny v. Silliman*, 28 U.S. (3 Pet.) 270, 277 (1830); *Campbell v. Haverhill*, 155 U.S. 610, 617 (1895); *Brady v. Daly*, 175 U.S. 148, 158 (1899); *McClaine v. Rankin*, 197 U.S. 154, 158 (1905); *Cope v. Anderson*, 331 U.S. 461, 463 (1947); *Chattanooga Foundry & Pipe Works v. City of Atlanta*, 203 U.S. 390, 397-98 (1906); *O'Sullivan v. Felix*, 233 U.S. 318 (1914); *Rawlings v. Ray*, 312 U.S. 96 (1941); *Holmberg v. Armbrecht*, 327 U.S. 392, 395 (1946); *Runyon v. McCrary*, 427 U.S. 160, 180-82 (1976); *DelCostello*, 462 U.S. at 158-59; *Wilson*, 471 U.S. at 266-67; *Agency Holding*, 483 U.S. at 147; *Owens v. Okure*, 488 U.S. 235 (1989); *Reed*, 488 U.S. at 323.

[5] By adopting state law, federal courts are relying on the states to balance the policy of repose with the substantive policy of providing a plaintiff reasonable time in which to bring a claim. *Wilson*, 471 U.S. at 271; and *id.* at 281 (O'Connor J., dissenting) ("In borrowing a state period of limitation for application to a federal cause of action, a federal court is relying on the State's wisdom in setting a limit . . . on the prosecution of a closely analogous claim.") (quoting *Johnson v. Railway Exp. Agency, Inc.*, 421 U.S. 454, 463-64 (1975)).

borrowing state law only "when a rule from elsewhere in federal law *clearly* provides a closer analogy than available state statutes, *and* when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial law making. . . . " *Id.* at 172 (emphasis added). Therefore, on rare occasions this Court will apply a federal limitations period where state law conflicts with or undermines federal policies.[6] Even then, this Court emphasizes that borrowing from federal law is a "narrow" and "closely circumscribed exception to the general rule that statutes of limitation are to be borrowed from state law. . . . '[R]esort to state law remains the norm for borrowing for limitations periods' ". *Reed*, 488 U.S. at 324 (quoting *DelCostello*, 462 U.S. at 171).

The first step in choosing the appropriate limitations period for § 10(b) claims is to determine whether such claims should be characterized uniformly or by a claim-by-claim approach. *See Agency Holding*, 483 U.S. at 147. Federal law governs this characterization. *Wilson v. Garcia*, 471 U.S. 261, 269-70 (1984). Second, this Court presumes that a state's statute of limitations will apply unless "federal law clearly provides a closer analogy" *and* "the federal policies at stake and the practicalities of litigation" make federal law "significantly more appropriate." *DelCostello*, 462 U.S. at 171-72.[7]

Applying this analysis here, this Court should uniformly characterize § 10(b) claims as actions for fraud and apply state statutes of limitations for common law fraud. Common law fraud provides a sufficiently close analogy to § 10b actions and is consistent with the federal policies at stake and the practicalities of litigation.

II. STATE COMMON LAW FRAUD STATUTES OF LIMITATION ARE SUFFICIENTLY ANALOGOUS, BEST IMPLEMENT THE FEDERAL POLICY BEHIND SECTION 10(b) AND ACCOMMODATE THE PRACTICALITIES OF LITIGATION.

A. All Private Actions Under Section 10(b) Should be Characterized the Same Way.

All the parties agree that private § 10(b) actions should be uniformly characterized in order "to avoid intolerable 'uncertainty and time-consuming litigation' " in determining the appropriate statute of limitations. *See Agency Holding*, 483 U.S. at 150 (quoting *Wilson*, 471 U.S. at 272).

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[6] *See Agency Holding*, 483 U.S. at 147 (applying the Clayton Act's limitation period, 15 U.S.C. § 15b, to civil RICO actions); *DelCostello*, 462 U.S. at 161 (limitation period of § 10(b) of the National Labor Relations Act, 29 U.S.C. § 160(b), applied to a claim for breach of a collective bargaining agreement/duty of fair representation); *McAllister v. Magnolia Petro. Co.*, 357 U.S. 221, 224 (1958) (federal limitation period of the Jones Act applied to claim for unseaworthiness); *Occidental Life Ins. Co. of Cal. v. EEOC*, 432 U.S. 355 (1977) (refusing to apply short, state statute of limitations to EEOC enforcement actions under the Civil Rights Act of 1964); *Holmberg v. Armbrecht*, 327 U.S. 392 (1946) (doctrine of laches, rather than state law, applied to action to enforce federal equitable remedy).

[7] Of course, any analogy to § 10(b) is "bound to be imperfect," *see Wilson*, 471 U.S. at 272, but "the mere fact that state law fails to provide a perfect analogy to the federal cause of action is never itself sufficient to justify the use of a federal statute of limitations, . . . " *Agency Holding*, 483 U.S. at 147. *See also DelCostello*, 462 U.S. at 171 ("We do not mean to suggest that federal courts should eschew use of state limitations periods any time state law fails to provide a perfect analogy."). The search is for a *sufficiently* analogous state statute of limitation which is consistent with federal policy and the practicalities of litigation.

B. Federal Policies and Practicalities of Litigation Are Best Served By a Longer, Not a Shorter, Statute of Limitations.

1. The Fundamental Purpose Behind the Federal Securities Laws Is to Protect Investors by Ensuring Full Disclosure, Preventing Fraud, and Providing Relief to Defrauded Investors.

The fundamental purpose of the Securities Act of 1933 and the Securities Exchange Act of 1934 is to ensure full disclosure to investors and to prevent and punish fraud. *Randall v. Loftsgaarden*, 478 U.S. 647, 664 (1986); *Ernst & Ernst*, 425 U.S. at 195; *S.E.C. v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963) ("a fundamental purpose [of the federal securities laws] . . . was to substitute a philosophy of full disclosure for the philosophy of *caveat emptor* . . . ").[8] This Court consistently holds that the securities laws are remedial in nature, to protect and provide relief to defrauded investors, and must be construed broadly to effectuate this purpose.[9] *Herman & MacLean*, 459 U.S. at 386-87; *Blue Chip Stamps*, 421 U.S. at 748; *Affiliated Ute Citizens of Utah v. United States*, 406 U.S. 128, 151 (1972); *Capital Gains*, 375 U.S. at 195.

Within this statutory framework, § 10(b) was designed as a "catchall" antifraud provision to enable the Commission to handle novel and unforeseen types of securities fraud. *Ernst*

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[8] *See also* S. Rep. No. 47, 73d Cong., 1st Sess. (Apr. 27, 1933), *reprinted in* 2 J. Ellenberger & E. Mahar, *Legislative History of the Securities Act of 1933 and Securities Exchange Act of 1934*, Item 17 (1973) ("The basic policy is that of informing the investor of the facts concerning securities to be offered for sale . . . and providing protection against fraud and misrepresentation.").

[9] The Court's broad interpretation of the antifraud provisions in the Acts is consistent with "Congressional intent that the courts construe the antifraud provisions of the federal securities laws broadly . . . " 98 Cong. Rec. H7760 (July 25, 1984) (remarks of Rep. Wirth).

& Ernst, 425 U.S. at 203. Ever since *Kardon v. National Gypsum Co.*, 69 F.Supp. 512 (E.D.Pa. 1946), implied a private right of action under § 10(b), it has become *the* most important weapon in combatting securities fraud.[10] Private § 10(b) actions constitute "an essential tool for enforcement of the 1934 Act's requirements," *Basic, Inc. v. Levinson*, 485 U.S. 224, 231 (1988), and provide a "necessary supplement to commission action," *Blue Chip Stamps*, 421 U.S. at 730 (quoting *J.I. Case Co. v. Borak*, 377 U.S. 426, 432 (1964)).[11]

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[10] Petitioner acknowledges that most security fraud cases are filed under § 10(b) and Rule 10b-5. *See* Pet.'s Br. at 21 ("§ 10(b) and Rule 10b-5 'may well be the most litigated provisions in the federal securities laws.' ") (quoting *S.E.C. v. National Sec., Inc.*, 393 U.S. 453, 465 (1969)). *See also* Guin & Donaldson, *The Insider Trading and Securities Fraud Enforcement Act: Has Congress Supplied a Limitations Period Appropriate For Use In Private 10b-5 Actions?*, 47 Wash. & Lee L. Rev. 541, 573 (1990); H. Bloomenthal, *Securities Law Handbook* § 12.01 at 317 (1987-88 ed.) (Rule 10b-5 has become "a utilitarian fraud remedy for private claimants").

[11] Private actions have become increasingly important as an enforcement tool in light of the dramatic growth of fraud and corruption in the nation's business community and financial institutions. *See, e.g.*, Schultz, *Ripoff Roundup – Beware: Investment Fraud in the '90's Will Claim A Wider Range of Victims*, Wall St. J., Oct. 19, 1990 at p. R24, col. 1 (*see infra* note 39); *White-Collar Crime: Booming Again – Economic Pressures, a New Permissiveness and Simple Greed Are Eroding Corporate Morality*, N.Y. Times, June 9, 1985, § III at 1 ("A corporate crime wave appears to be exploding across the nation. Not since the mid-1970s when a series of foreign corporate bribes and illegal political contributions shocked the body politic, have there been so many deep gashes in corporate America's moral armor"); *Captain Money and The Golden Girl*, Forbes, July 1, 1985 at 72 ("We live in an era of unprecedented financial

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Therefore, federal policy is to encourage private litigation of § 10(b) claims. *Basic*, 485 U.S. at 245 ("facilitating Rule 10b-5 litigation supports the congressional policy embodied in the 1934 Act"); *see also Pinter v. Dahl*, 486 U.S. 622, 633

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fakery. Billions of dollars of worthless securities and financial instruments are being foisted on the public").

The SEC and the states simply do not have the resources to stem the growing tide of corruption. *See Inundated Agency, Busy SEC Must Let Many Cases, Filings Go Uninvestigated*, Wall St. J., Dec. 16, 1985 at 1:

> "The SEC is horribly overmatched by the bad guys in the marketplace," declares Royce Griffin, the president of the North American Securities Administrators Association. . . .
>
> But concerns about the SEC's workload are growing. A recent report by an American Bar Association task force says the enforcement staff may be too small "for the Commission to effectively discharge its statutory responsibilities. . . . "
>
> Chairman Shad points out that the SEC isn't the sole defense against false or misleading financial statements. If anything is seriously amiss, he contends, "you can be sure the private bar will be in there with class-action suits."

See also Bateman Eichler, Hill Richards, Inc. v. Berner, 472 U.S. 299, 315 (1985) ("The SEC has advised us that it 'does not have the resources to police the industry sufficiently . . . ' "); H.R. Rep. No. 355, 98th Cong. 1st Sess. 6 (1983), *reprinted in* 3 Fed. Bar Ass'n. Sec. L. Comm., *Federal Securities Law Legislative History 1933-1982*, Item 249, p. 4889 ("in recent years, the securities markets have grown dramatically in size and complexity, while Commission enforcement resources have declined"); 98 Cong. Rec. H2982 (daily ed. May 17, 1983) ("The SEC historically has been a lean agency, and in recent years, the areas within its jurisdiction have expanded dramatically. . . . In the three years since the SEC's last authorization, the value of [registered] public offerings . . . has risen almost 100 percent. The number of investment companies has risen almost 40 percent, and investment company assets have risen almost 200 percent. The volume of shares traded in the markets has grown 80 percent. The number of broker-dealers has grown 20 percent. . . . The SEC has told us that problems in the area of financial statement fraud are growing dramatically . . . ") (remarks of Rep. Wirth).

(1988) (recognizing "the congressional policy favoring private suits as an important mode of enforcing federal securities statutes").[12] For these reasons, the "policies of the federal securities laws are best served by a longer, not a shorter, statute of limitations." *Berry Petro. Co. v. Adams & Peck*, 518 F.2d 402, 409 (2d Cir. 1975) (quoting *United Cal. Bank v. Salik*, 481 F.2d 1012, 1015 (9th Cir. 1973), *cert. denied*, 414 U.S. 1004 (1973)).

2. The Practicalities of Section 10(b) Litigation Require a Discovery-Based Statute of Limitations that Is Not Subject to a Three Year Period of Repose.

The distinguishing feature of § 10(b) litigation is the requirement of scienter.[13] *See Ernst & Ernst*, 425 U.S. at 199, 201. It is the very nature of fraud that it is difficult to detect by virtue of the malfeasor's intentional acts or omissions. *See* American Bar Association, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 654 (1986) ("*ABA Task Force Report*") ("such concealment is inherent in most securities fraud cases"). Consequently, even the most sophisticated plaintiffs often are not able to "discover fraud until long after its perpetration," especially in

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[12] Legislative history to the Insider Trading Act, 15 U.S.C. § 78t-1, reveals Congress' awareness of and approval that private § 10b claims "have traditionally served as an important supplement to the Commission's enforcement of federal securities laws." H.R. Rep. No. 910, 100th Cong., 2d Sess. 26, (testimony of S.E.C. Chairman Ruder) *reprinted in* 1988 U.S. Code Cong. & Admin. News 6063.

[13] While § 9(e) of the 1934 Act, 15 U.S.C. § 78i(e), may require scienter, it applies to a very limited class of defendants and transactions. Further, § 9(e) violations, as well as other stock market fraud, do not go long unnoticed due to the SEC's record-keeping and investigatory functions and the degree to which the national exchanges are scrutinized.

complex, interstate investment schemes.[14] *Id.* at 656. For example, in "Ponzi" schemes, bond defaults, limited partnerships and other complex investment scenarios, it may take significantly more than three years to detect any wrongdoing.[15] Investors can be easily deceived with continued promises of high returns, periodic payments of "profits" or

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[14] The SEC confirms that "as the securities markets have grown in size and complexity, frauds have become increasingly difficult to discover." SEC's *Amicus* Br. at 24. "Indeed, even the SEC with all its investigative resources and statutory powers, including compulsory investigative processes, does not complete its investigations, on average, in less than 2.25 years." *Id.* at 24, n.37. In its experience it has found that "a considerable number of frauds are simply not detected within [three years]." *Id.* at 25. Therefore, it is not simply "the most trusting or somnolent investors," *Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1392 (7th Cir. 1990), *cert. pending*, (No. 90-526), that do not discover fraud within three years. Often times, even reviewing published financial statements may not reveal fraud. Moreover, investors do not invest with the thought of looking for fraud especially when stockbrokers or general partners have a fiduciary obligation of full disclosure. If investors then receive audited financial statements, showing assets, growth earnings, gains and the like, they will be even less likely to look for fraud. Yet, it is precisely this type of information that will cause a person to be "somnolent" even though this information actually might be hiding a massive fraud.

[15] "Ponzi" schemes are specifically designed to deceive the investor into thinking he is receiving a profit on his investment when actually he is only receiving money invested by other victims. For example, in *In re Home-Stake Production Co. Sec. Litig.*, 76 F.R.D. 351 (N.D.Okla. 1977), investors in oil and gas drilling operations received quarterly progress reports indicating that substantial oil was being produced, and received quarterly "profits" which were actually money received from subsequent investors. Even a lawsuit by the SEC did not reveal the fraud. For other cases involving "Ponzi" schemes, see Guin & Donaldson, *supra* note 10, at 569 n.168. With a three year period of repose, "the malfeasor can insulate himself from liabilities simply by paying the phoney return until the statute expires." *Id.* at 569. *See generally* Bond Investors Association ("BIA") *Amicus* Br. at Section I. for a thorough discussion of "Ponzi" schemes and bond defaults.

glowing, audited financial statements. Accordingly, this Court has twice recognized that the longer limitations periods traditionally available under state law are consistent with the scienter requirement of § 10(b). *Ernst & Ernst*, 425 U.S. at 210, n.29; *Herman & MacLean*, 459 U.S. at 384 n.18.

In light of the investor-oriented, remedial purpose of the federal securities laws, the limitations period applied to § 10(b) claims must take into account the practical difficulty of discovering fraud and provide a reasonable amount of time for a plaintiff to file a claim. This is precisely the practicalities of litigation this Court has consistently examined when determining whether state law provides an appropriate statute of limitations. In *DelCostello*, this Court applied the six month limitation period of § 10(b) of the N.L.R.A. because state limitation periods for actions to vacate an arbitration award (typically between 10 and 90 days) are simply too short "to provide an aggrieved employee with a satisfactory opportunity to vindicate his rights under § 301 and the fair representation doctrine." 462 U.S. at 166 (footnote omitted). State law suffered from these "flaws . . . of practical application" and thereby frustrated the federal policy of allowing an employee sufficient opportunity to bring a claim.[16] *Id.* at 165; *see also Reed*, 488 U.S. at 328, n.4. In *Agency Holding*, this Court applied the limitations period of the Clayton Act to civil RICO claims partly for the reason that the states' limitation periods were "unduly short" to allow a plaintiff to bring a claim and thus, "would thwart the

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[16] The Court also considered and rejected state limitation periods for legal malpractice for the reason such limitation periods (from two to six years) are too long and conflict–with the policy of "rapid final resolution of labor disputes. . . . " *DelCostello*, 462 U.S. at 168. Contrary to securities fraud, the type of injury involved in *DelCostello* (breach of a collective bargaining agreement and the duty of fair representation) does not involve the issue of discovery.

legislative purpose of creating an effective remedy."[17] 483 U.S. at 154. In *Occidental Life Ins. Co. of Cal. v. EEOC*, 432 U.S. 355 (1977), this Court refused to apply a short, state limitations period to EEOC enforcement actions. The one year, state limitations period would have placed too great a burden on the EEOC to bring such actions and, therefore, was "inconsistent with the congressional intent underlying the" Civil Rights Act of 1964. 432 U.S. at 369. In *McAllister v. Magnolia Petro. Co.*, 357 U.S. 221 (1958), this Court applied federal law because the shorter, state limitations period did not accommodate "the practicalities of admiralty personal injury litigation" and did not allow a plaintiff sufficient time in which to bring an unseaworthiness claim. 357 U.S. at 224. In *Holmberg v. Armbrecht*, 327 U.S. 392 (1946), state statutes of limitations were inappropriate because they could potentially cut off an action to enforce a federal equitable remedy. 327 U.S. at 397. In all of these instances, this Court applied a *longer*, federal limitations period instead of a shorter, state

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[17] Another factor considered was that RICO encompasses a wide variety of divergent federal and state claims which could potentially provide an analogy for statute of limitations purposes. Civil RICO claims include "nine state law felonies and violations of over 25 federal statutes, including those prohibiting bribery, counterfeiting, embezzlement of pension funds, gambling offenses, obstruction of justice, interstate transportation of stolen property, and labor crimes," *Agency Holding*, 483 U.S. at 149 (quoting *A.J. Cunningham Packing Corp. v. Congress Fin. Corp.*, 792 F.2d 330, 337 (3rd Cir. 1986) (Sloviter, J., concurring)) and can be "analogized to breach of contract, fraud, conversion, tortious interference with business relations, misappropriation of trade secrets, unfair competition, usury, disparagement, etc.. . . . " *Id.* (quoting *Malley-Duff & Assocs., Inc. v. Crown Life Ins. Co.*, 792 F.2d 341, 348 (3d Cir. 1986) *aff'd*, 483 U.S. 143 (1987)). Here, while § 10(b) can be analogized to common law fraud, state blue sky laws, breach of fiduciary duty and negligence, the galaxy of analogous claims "is not as impressive as under RICO as it inevitably comes back to some form of fraud, manipulation or deceit." 11 H. Bloomenthal, *Securities & Federal Corporate Law Report* (hereinafter "SFCLA"), at 10 (Feb. 1989).

period which would have thwarted federal policy by not allowing a plaintiff sufficient time to seek redress under the applicable statute.

Courts, Congress and state legislatures have recognized these practicalities in fraud claims. In light of the practical difficulty of discovering fraud, courts have almost universally applied a "discovery" rule. *See* Shapiro & Blouner, *Securities Litigation in the Aftermath of In re Data Access Securities Litigation*, 24 New Engl. L. Rev. 537, 549-50 (1989). The clock does not begin to run until plaintiff knew or should have known of the fraud. The federal version of this rule, the doctrine of equitable tolling, has long been recognized by this Court and is "read into every federal statute of limitation," particularly "as to fraud." *Holmberg*, 327 U.S. at 397; *see also Bailey v. Glover*, 88 U.S. (21 Wall.) 342, 348 (1874); *Cook v. Avien, Inc.*, 573 F.2d 685, 694-5 (1st Cir. 1978); *United States v. Lovknit Mfg. Co.*, 189 F.2d 454, 457 (5th Cir.) ("actions for a *fraud* do not ordinarily accrue till the fraud is discovered or should with diligence have been discovered") (Court's emphasis), *cert. denied*, 342 U.S. 896 (1951). In the Interstate Land Sales Act, Congress recognized the importance of a limitations period that runs from discovery and is not subject to a period of repose. *See* 15 U.S.C. § 1711(a)(2). *See infra* Section III.B.1. Similarly, state legislatures have long established that the limitations period for fraud does not begin to run until constructive discovery, *see* Shapiro, *supra*, at 549-50, and recently, several states have amended their blue sky laws to allow a plaintiff *more* time in which to bring a claim.[18] Any argument that a longer statute of limitations

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[18] Within the last several years, at least six states have *extended* their statutes of limitations for blue sky actions. Arkansas extended its statute from two years to five years from sale. *Compare* former Ark. Stat. Ann. § 67-1256(e) (1966) *with* Ark. Stat. Ann. § 23-42-106(f) (1987). Florida entirely eliminated its "two years from sale" limitation. *Compare*

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will permit a plaintiff to delay filing a claim after fraud has been discovered, hoping the value will go up but intending to shift further risk of loss to potential defendants, is of no avail. Courts have the ability to deal with any such abuse. *See Randall*, 478 U.S. at 666.

C. Common Law Fraud Is Sufficiently Analogous to Section 10(b) and Is Consistent With Policies and Practicalities of Securities Litigation.

The characterization of § 10(b) claims "for statute of limitations purposes is derived from the elements of the cause of action, and Congress' purpose in providing it." *See Wilson*, 471 U.S. at 268. Section 10(b) is a fraud-based action. Its elements parallel those of common law fraud. Each requires proof of a representation, its falsity or material omission, reliance thereon, damages caused by the wrongdoing and scienter on the part of defendant.[19] *See Ernst & Ernst*, 425

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former Fla. Stat. § 301.1 (1976) *with* Fla. Stat. § 517.301 (1988). Hawaii recently adopted a rule of two years from discovery, but no more than seven years from sale. Hawaii Rev. Stat. § 485-20.5 (1985). Indiana increased its statutory period from "two years from sale" to three years from discovery. *Compare* former Ind. Code § 23-2-1-19(e) (1967) *with* Ind. Code § 23-2-1-19(g) (1989). Oregon extended its statute of limitations from "three years after the sale" to two years from discovery or three years from sale, whichever is longer. *Compare* former ORS 59.115(5) (1983) *with* ORS 59.115(5) (1989). Vermont lengthened its period from "two years from sale," to three years from discovery, or six years from the transaction, whichever occurs first. *Compare* former Vt. Stat. Ann. tit. 9, § 4225 (1984) *with* Vt. Stat. Ann. tit. 9, § 4240(f) (1990 Supp.). Moreover, at least within the last ten years, no state has *shortened* its statute of limitations for blue sky violations.

[19] "[A] claim under Rule 10b-5 certainly has some relationship" to the tort of deceit and misrepresentation. *Blue Chip Stamps*, 421 U.S. at 744. Rule 10b-5 and common law fraud differ primarily in that, for a Rule 10b-5 case, the fraud must be "in connection with the purchase or

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U.S. at 193; *Basic*, 485 U.S. at 243; *see generally* L. Loss, *Fundamentals of Securities Litigation* 712-23 (2d. ed. 1988) ("Loss"); *Prosser and Keeton on the Law of Torts* § 105 at 728 (W. Keeton 5th ed. 1984). Further, both common law fraud and § 10(b) apply to those directly at fault and to those

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sale" of a security, *see id.*, and a plaintiff is subject to a lighter evidentiary burden. A plaintiff need only prove securities fraud by a preponderance of the evidence, rather than by clear and convincing evidence, *Herman & MacLean*, 459 U.S. at 390, and there is a rebuttable presumption of reliance if there is a duty to disclose, fraud-on-the-market or a material misstatement or omission in a proxy statement, *Basic*, 485 U.S. at 245, 250. In light of the investor-oriented, remedial purpose of the federal securities laws, these evidentiary burdens were relaxed to enable a plaintiff to more easily prove securities fraud and to extend liability "to a broader reach than the common law had previously permitted. . . . " *Id.* at 253 (White, J., concurring in part, dissenting in part); *see Herman & MacLean*, 459 U.S. at 390 (lighter standard of proof justified by fundamental purpose of securities laws to protect investors: "If they prove that it is more likely than not that they were defrauded, they should recover."). Thus, plaintiffs are able to bring class action suits for nationwide securities fraud or maintain actions for securities bought on a national market, where such actions would not be possible under traditional common law fraud theories.

Petitioner uses these procedural distinctions between § 10(b) and common law fraud to argue that common law fraud does not provide a sufficient analogy. Instead, Petitioner argues for a draconian one year limitation/three year repose period which would make it harder for plaintiffs to obtain *any* relief for fraud under the federal securities laws. Simply because § 10(b) arises out of a different historical context than common law fraud and is subject to fewer evidentiary and procedural burdens, is not a sufficient reason to look to federal law and ignore over 150 years of precedent and 45 years of congressional acquiescence of looking to state law for the applicable statute of limitations. The inquiry is whether applying common law fraud limitation periods is consistent with the policy of preventing fraud and providing relief to defrauded investors, and accommodates the practicalities of § 10(b) litigation.

who aid and abet the primary wrongdoer.[20] In contrast, the federal express remedies apply only to specific categories of defendants. *See infra* Section III.A. In light of the identity of purpose and substantive elements between § 10(b) and common law fraud, common law fraud is sufficiently analogous to § 10(b) for statute of limitations purposes.

Statutes of limitations for common law fraud are designed to accommodate the same practicalities which face a § 10(b) plaintiff. In both, the requirement of scienter necessarily involves a situation where the wrongdoing goes undetected by virtue of the intentional acts or omission of the defendant.[21] Therefore, these limitation periods are of sufficient length[22] to accommodate the practicalities of § 10(b) litigation, and promote the federal policy of providing relief to defrauded investors and facilitating private enforcement of the securities laws.

1. The *Wilson* Approach Should Be Applied to Achieve a Necessary Degree of Uniformity and Certainty.

In *Wilson*, this Court balanced interests in uniformity with the traditional rule of borrowing state law by ruling that federal courts should apply personal injury statute of limitations to § 1983 claims under the Civil Rights Act of 1871, 42

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[20] *See* Restatement (Second) of Torts § 876 (1979); *Harmsen v. Smith*, 693 F.2d 932, 943 (9th Cir. 1982), *cert. denied*, 464 U.S. 822 (1983); *Saltzman v. Zern*, 407 F.Supp. 49, 53-57 (E.D. Pa. 1976); Loss, *supra*, at 1020-21. In *Pinter v. Dahl*, 486 U.S. 622, 654 (1987), this Court rejected the "substantial factor" test in determining a "seller" under § 12(1) of the 1933 Act.

[21] Because the tort of deceit contemplated situations involving face-to-face transactions, *Basic*, 485 U.S. at 243-4, the fraudulent act should be discovered, theoretically, sooner than with a § 10(b) violation. Therefore, a § 10(b) plaintiff should certainly not be provided *less* time than what is allowed for common law fraud in which to discover fraud and bring a claim.

[22] Common law fraud statutes of limitation are, generally, two to six years and start to run when plaintiff discovers or reasonably should have discovered the fraud. *See* ABA Task Force Report, *supra*, at 650.

U.S.C. § 1983. Section 1983 claims can be analogized to a "wide diversity of claims." *Wilson*, 471 U.S. at 275. Analogizing § 1983 actions to personal injury claims best covered the broad range of tort remedies embraced by § 1983 and, thus, was consistent with the "statute's remedial purpose." *Id.* at 272. By uniformly characterizing § 1983 claims, this Court accommodated "[t]he federal interests in uniformity, certainty, and the minimization of unnecessary litigation. . . . " *Id.* at 275; *see also Reed*, 488 U.S. at 326 (characterizing § 101(a)(2) claims under Labor-Management Reporting and Disclosure Act as personal injury claims resolved problem of uncertainty and lack of uniformity in statutes of limitation).

Here, uniform characterization of § 10(b) actions as involving claims for common law fraud "minimizes the risk that the choice of a state statute of limitations would not fairly serve the federal interests" at issue or would not accommodate the practicalities of litigation. *Wilson*, 471 U.S. at 279.[23] Therefore, the concern for

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[23] Even in cases involving several states, a conflict of law analysis may be unnecessary. *Brick v. Dominion Mortgage & Realty Trust*, 442 F.Supp. 283, 300 (W.D.N.Y. 1977). The statute of limitations of the forum state will govern. *See, e.g., Nortek, Inc. v. Alexander Grant & Co.*, 532 F.2d 1013, 1015 (5th Cir. 1976), *cert. denied*, 429 U.S. 1042 (1977). Use of the forum state statute of limitations is constitutional. *Sun Oil Co. v. Wortman*, 486 U.S. 717 (1988). Because state common law fraud statutes of limitations are discovery-based, it would be unusual for a case to involve plaintiffs from multiple states and a choice of law issue on the statutes of limitations that is material to the outcome. Once a plaintiff discovers fraud it is unlikely he will wait more than two years to file suit. The Ninth Circuit, which applies the forum state's common law fraud statute of limitations, *see infra*, note 63, has not encountered the problems that the Third and Seventh Circuits had in choosing the appropriate statute of limitations. Neither party has cited a case where multiple statutes of limitations were applied other than *Kronfeld v. Advest, Inc.*, 675 F.Supp. 1449 (S.D.N.Y. 1987), in which the court had no trouble managing the issue. Other cases have refused to deny class certification on the issue and have suggested that a single statute of limitations could be applied in a case involving diverse plaintiffs. *See In re Nat'l Student Marketing Litig.*, Fed. Sec. L. Rep., (CCH) ¶ 97,926 (D.D.C. March 26, 1981); *State Teachers Retirement Bd. v. Fluor Corp.*, 80 F.R.D. 142 (S.D.N.Y. 1978).

certainty and uniformity can be resolved while accommodating the policies and practicalities involved in § 10(b).

D. State Blue Sky Statutes Are Not as Analogous as Common Law Fraud.

Many state blue sky statutes differ significantly from § 10(b) and, thus, are not sufficient analogies. Most state blue sky laws which provide for private causes of action are modeled after § 410(a) of the Uniform Securities Act, which is itself modeled after § 12 of the 1933 Act.[24] Loss, *supra*, at 878; *see, e.g., Capri v. Murphy*, 856 F.2d 473, 478 (2d Cir. 1988). Like § 12, but unlike § 10(b), most blue sky laws do not require proof of reliance, causation or scienter, *see* Guin & Donaldson, *supra* note 10, at 580-81, and are quite limited in scope.[25] Accordingly, the limitations periods in blue sky laws are not as appropriate as common law fraud statutes of limitations for § 10(b) claims.

III. THE EXPRESS FEDERAL REMEDIES ARE NOT CLEARLY MORE ANALOGOUS THAN STATE LAW, AND APPLYING A ONE YEAR/THREE YEAR LIMITATIONS PERIOD WOULD CONFLICT WITH FEDERAL POLICY AND THE PRACTICALITIES OF LITIGATION.

The presumption of borrowing state statutes of limitations is overcome only if "federal law *clearly* provides a closer analogy" than state law and is consistent with federal policy and practicalities of litigation. *DelCostello*, 462 U.S. at 172 (emphasis added). The express actions under the 1933

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[24] Since most blue sky private remedies are identical to § 12, it is not possible for the express remedies of the Acts to be *more* analogous than these statutes.

[25] Under some blue sky laws only purchasers of securities can sue for fraud, *see Data Access*, 843 F.2d at 1544, others require the defendant to be a seller or require privity, and others do not cover the broad scope of activity prohibited by § 10(b). *See generally* Shapiro & Blauner, *supra*, at 563. Generally, blue sky statutes vary considerably from state to state and come "in a variety of shapes and sizes." Loss, *supra*, at 877-79.

and 1934 Acts[26] are not clearly more analogous than common law fraud. They do not require the same elements of proof as in § 10(b) cases, do not address the same type of culpable conduct, and cover a much narrower class of persons and activities. The unduly short three year period of repose would clearly frustrate the federal policies of ensuring complete disclosure, providing relief to defrauded investors and facilitating private enforcement. Further, the practical difficulty of discovering fraud within three years, recently noted by Congress, mandates against the imposition of a three year statute of repose.

A. The One Year/Three Year Limitations Period of the Express Remedies of the 1933 and 1934 Acts Does Not Clearly Provide a Closer Analogy than Common Law Fraud.

Sections 11 and 12 of the 1933 Act and § 18 of the 1934 Act, unlike § 10(b), do not require proof of scienter, reliance

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[26] The 1933 Act provides express rights of action under § 11, 15 U.S.C. § 77k, which prohibits misleading statements or omissions in a registration statement, § 12(1), 15 U.S.C. § 77l(1), which prohibits the unlawful sale of an unregistered security and § 12(2), 15 U.S.C. § 77l(2), which prohibits the sale of a security through false or misleading statements. Section 13 of the 1933 Act, 15 U.S.C. § 77m, provides the limitations period for §§ 11 and 12.

The 1934 Act provides for express causes of action under § 9(e), 15 U.S.C. § 78i(e); § 16(b), 15 U.S.C. § 78p(b); § 18(a), 15 U.S.C. § 78r(a), and § 29(b), 15 U.S.C. § 78cc(b). Section 9(e) prohibits manipulation of securities prices by brokers or dealers on national securities exchanges. Section 16 prohibits unlawful profits from the purchase or sale of securities within six months, i.e., short-swing profits. Section 18(a) imposes liability for misleading statements in any document filed with the SEC. These sections each provide for a variation of a one year from discovery/three year from sale statute of limitations, except for § 16(b) which requires that suits be brought no later than two years after the unlawful profit was realized. Petitioner concedes that § 16(b) is not an appropriate choice for § 10(b) claims. Pet.'s Br. at 43.

or causation, and place upon the defendant the burden of establishing good faith. *See, e.g., Currie v. Cayman Resources Corp.*, 835 F.2d 780, 782 (11th Cir. 1988); *see generally* Loss, *supra*, at 883-900. These are strict liability and negligence provisions and do not require proof of an intent to deceive, manipulate or defraud.[27] Further, the class of potential

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[27] A relatively short statute of repose may be appropriate where a person may be found liable for conduct that does not involve scienter and the defendant has the burden of proving due diligence. The situation is different with § 10(b) (and with common law fraud) where a defendant intentionally commits fraud and the plaintiff has the burden of proof on all elements of the claim. The legislative history of the 1934 Act indicates that Congress enacted the short, three year statute of repose in light of the relatively light burden placed upon a plaintiff in relation to the express remedies. As Petitioner points out, during Senate debate on the appropriate limitations period, Senator Barkley stressed the difficulties in discovering fraud within three years:

> It would be manifestly unfair . . . to limit any damaged party to 1 year or 2 years or 3 years in the bringing of a suit, because it may sometimes take 4 or 5 years to discover that a fraud has been committed in a statement of facts or in the omission of a statement with reference to a share of stock or a report which may be made based upon the condition of a company.

Pet.'s Br. at 40, n.58 (quoting 78 Cong. Rec. 8201 (May 7, 1934) (Statement of Sen. Barkley)). But Petitioner failed to include the following response by Senator Austin:

> I inquire of the Senator from Kentucky whether he does not recognize another exceptional circumstance in that the burden of proof is shifted around on the question of knowledge or wilfulness in a misrepresentation. The committee has put the burden upon the defendant, so that in this case the plaintiff does not have to spend any time going out and seeking his evidence. All he has to prove is the fact of misrepresentation.

78 Cong. Rec. 8201 (1934); *see also Herman & MacLean*, 459 U.S. at 382 ("§ 11 places a relatively minimal burden on a plaintiff. In contrast, § 10(b) . . . requires . . . a heavier burden to establish a cause of action.").

plaintiffs and defendants is much narrower than under § 10(b).[28]

Petitioner contends § 9 of the 1934 Act is the "closest analog for § 10(b)." Pet.'s Br. at 34. While § 9 may require scienter[29] it also is too limited for purposes of analogizing to § 10(b). This section applies only to brokers or dealers who deal directly with investors and only to securities registered on a national securities exchange. *See generally* 5 A. Jacobs, *Litigation and Practice Under Rule 10b-5*, § 3.02[c], (rev. ed. 1990). Accordingly, § 9(e) is not an effective remedy for defrauded investors and "has been a dead letter so far as producing recoveries is concerned." Loss, *supra*, at 920. *See also* 11 SFCLR, *supra* note 17, at 18 ("Neither Section 9(e) nor Section 18(a) . . . has spawned much litigation.").

Violations of the express remedies, especially § 9, are generally discovered in a relatively short amount of time given the degree to which the national securities exchanges are scrutinized and the extent to which the SEC monitors

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[28] Section 11 claims can only be brought by a purchaser of a registered security, *see Herman & MacLean*, 459 U.S. at 382, and the universe of potential defendants is limited to persons who signed the registration statement, directors or partners of the issuer at the time the statement was filed, underwriters and experts who prepared or certified any portion of the statement. Actions under § 12 may be brought only by purchasers against sellers of a security. *See Pinter*, 486 U.S. at 641-47. Likewise, § 18 applies only to persons who make, or cause to be made, false filings with the SEC. Section 29(b) is also too limited in scope. It applies only to contracts and merely provides a remedy of rescission.

[29] *But see* Loss, *supra*, at 920 ("[a]lthough § 9(e), apart from some of the substantive provisions in § 9(a)-(d), does not require proof of scienter . . . "). Under § 9(e) a plaintiff must show that the defendant "willfully" participated in the manipulation of stock prices. However, this does not impose a difficult burden if there is any proof the defendant participated in the manipulation, in light of the loose manner in which courts have interpreted "willfully." *Id.* at 921. Yet, at the same time, § 9(e) has a strict causation requirement which is difficult for plaintiffs to satisfy. *Id.* at 920.

publicly traded securities. *See* SEC *Amicus* Br. at 19 n.27; *see also* Sontag, *Time May Not Be On Their Side*, Nat'l. L. J., Dec. 31, 1990, at 1, col. 3 ("stock market frauds . . . often are uncovered relatively early by market forces . . . "). Therefore, the short, three year period of repose is appropriate for the express actions given the ease of early detection of these violations,[30] the relatively light burden placed on plaintiffs to establish liability and the rather narrow class of persons and contexts in which the express remedies apply.[31]

1. The Express Statutes of Limitations Differ from Each Other.

Not only are the express rights of action not clearly more analogous to § 10(b), no two limitation periods are alike.[32]

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[30] Section 10(b) actions, on the other hand, often involve fraud in relation to unregistered and exempt securities, such as limited partnerships (as in this case), municipal bonds, tax shelters, real estate transactions, venture capital deals and so forth. These private transactions do not benefit from the two levels of institutional oversight provided by the SEC and the national exchanges. Thus, investors often have no access to any organized and regulated method of ongoing reporting and are provided information only at the whim of the promoter.

[31] *See infra*, n.38.

[32] The limitation periods for §§ 11 and 12 are provided in § 13 of the 1933 Act, 15 U.S.C. § 77m. In a § 11 action the period begins to run with the discovery of the untrue statement or omission, or after such discovery should have been made with reasonable diligence; but an action cannot be filed "more than three years after the security was bona fide offered to the public." The period for a § 12(1) action is one year after "the violation," and no more than three years after a bona fide offering to the public. Under § 12(2) the limitation period starts, as in § 11, one year after the discovery of the untrue statement or omission, or after such discovery should have been made; but cannot be brought more than three years after sale.

Under the 1934 Act, the period for § 9(e) begins one year after discovery of the facts constituting the violation, but no more than "three

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Simply adopting a uniform one year/three year period will not lead to uniformity or certainty, but will lead to confusion as to *which* rule to apply. This is demonstrated by the holdings in *Data Access*, *supra*; *Short*, *supra*, and *Ceres Partners v. GEL Assocs.*, 918 F.2d 349 (2d Cir. 1990). *Data Access* held that the applicable statute of limitations for § 10(b) is "one year after the plaintiff discovers the facts constituting the violation, and in no event more than three years after such violation." 843 F.2d at 1550. This limitation period has no exact counterpart in either Act. *Short*, on the other hand, applied the limitation period of § 12(2), 908 F.2d at 1390-91, which allows for constructive discovery, contrary to § 9(e) and *Data Access*. *Ceres Partners* held that the limitation periods of §§ 9(e) and 18(a) govern Rule 10b-5 actions. 918 F.2d at 364. However, as discussed *supra*, the limitation periods for those sections are not identical.[33] *See also Davis v. Birr, Wilson & Co., Inc.*, 839 F.2d 1369, 1376 (9th Cir. 1988) (Aldisert, J., concurring) (recommending the adoption of a rule limiting § 10(b) to "one year after the plaintiff discovers the facts, and in no event more than three years after the transaction in

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years after such violation." 15 U.S.C. § 78i(e). However, with § 18(c), the period starts one year after the discovery of the facts constituting the "cause of action," but no more than three years after "such cause of action accrued." 15 U.S.C. § 78r(c). An action to rescind a contract under § 29 must be brought within one year after discovering that a sale or purchase involved a violation but no more than three years after such violation. 15 U.S.C. § 78cc(b). The variation in these limitation periods demonstrates Congress' intent to establish limitation periods that are specifically suited to each particular remedy.

[33] The limitation periods for §§ 9(e) and 18(a) begin with discovery of the facts constituting the cause of action, but § 9(e) has a three year repose after the "violation," while § 18(c) has a three year repose after the "cause of action accrued." The point at which a violation occurs is not necessarily when a cause of action accrues. *See* SEC *Amicus* Br. at 21, n.30.

question" which is not identical to any of the express limitation periods or to the rules adopted in the Second, Third and Seventh Circuits).[34]

2. Private Actions Under Section 10(b) Have Been Shaped by this Court Upon the Assumption that the Applicable Limitation Period Is Longer than the Express Limitation Periods.

This Court has twice acknowledged that the express limitation periods do not apply to § 10(b) private actions. *See Ernst & Ernst*, 425 U.S. at 210, n.29; *Herman & MacLean*, 459 U.S. at 384, n.18. While the Court did not specifically address this issue, the holdings in these cases were premised upon the assumption that the limitation period for § 10(b) actions are longer than for the express remedies. Scienter was considered appropriate for Rule 10b-5 actions, *Ernst & Ernst*, 425 U.S. at 208-210, and §§ 10(b) and 11 were held to be cumulative, *Herman & MacLean*, 459 U.S. at 384, primarily because the procedural restrictions within the express actions (short limitations period and a bond requirement)[35] do not

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[34] Courts not only disagree over *which* one year/three year period to apply, but also in how they interpret the same limitations period. For instance, courts are divided whether the one year period in § 12(1) is subject to a discovery rule or the equitable tolling doctrine for fraudulent concealment. *See* Loss, *supra*, at 989. Further, the limitation periods in the 1934 Act do not contain a due diligence requirement, but several courts have nevertheless read such a requirement into the Act. *See, e.g., Goldenberg v. Bache & Co.*, 270 F.2d 675, 681 (5th Cir. 1959) (reasonable diligence requirement read into one year discovery period of § 29(b)) (citing *Holmberg*, 327 U.S. 392); *Lorenz v. Watson*, 258 F.Supp. 724, 734-35 (E.D. Pa. 1966) (reasonable diligence requirement read into § 15(c)(1)); *see also* 11 SFCLR, *supra* note 17, at 19 (due diligence requirement should be read into 1934 Act since this is consistent with congressional intent).

[35] These cases compared § 10(b) with §§ 11 and 12. However, §§ 9 and 18 contain the same procedural restrictions. *See* 15 U.S.C. §§ 78i(e), 78r(a), (c).

apply to Rule 10b-5 claims.[36] Since the law of § 10(b) private actions has been shaped by the assumption that the one year/three year limitations periods do *not apply*, it is fundamentally incorrect to suggest otherwise. Petitioner's argument simply ignores this historical development of § 10(b) private actions.[37]

B. A Three Year Period of Repose Would Undermine Federal Policy and Ignore the Practicalities of Litigation.

Applying a three year period of repose to § 10(b) actions would effectively undermine its remedial purpose to

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[36] This Court found it unpersuasive that there is overlap between §§ 10(b) and 11. Such overlap is to be expected, but this does not preclude that § 10(b) applies in numerous contexts in which § 11 cannot. *See Herman & MacLean*, 459 U.S. at 382-83. Similarly, Petitioner's argument that because there is overlap between § 10(b) and the express remedies, § 10(b) is substantively similar to the express actions is unpersuasive. There are numerous contexts in which § 10(b) applies but not the express actions. *See infra*, n.38.

[37] The theme of Petitioner's argument is that had the 73rd Congress provided for a private remedy for § 10(b), it would have enacted a one year/three year limitations period. Consequently, they focus on the legislative history behind the Acts. None of this legislative history indicates that, had Congress passed a fraud statute containing all of the elements of a § 10(b) claim, it would have applied a one year/three year limitations period. Petitioner's mode of analysis is inherently misguided. There is no indication the 73rd Congress or the SEC considered the possibility of a private right of action under § 10(b) or Rule 10b-5. *See Blue Chip Stamps*, 421 U.S. at 730, 737. There simply is no legislative intent by which to "divine" what statute of limitations Congress would have enacted. *Id. See DelCostello*, 462 U.S. at 158 n.12 ("[m]ore often . . . Congress has not given any express consideration to the problem of limitations periods."). This is precisely why this Court developed the test outlined in *DelCostello*. This Court has never tried to resolve this issue by trying to guess what Congress would have done had it provided for a limitations period. On the contrary, the presumption is that Congress intends by its silence that courts apply state law. *Agency Holding*, 483 U.S. at 147. Legislative intent is examined only to determine whether state law is consistent with the policies contained in the statute.

encourage full disclosure, prevent fraud and provide relief to defrauded persons. It would also conflict with the policy of facilitating private enforcement of the federal securities laws. Section 10(b) applies to a wide variety of ~~situ~~ations to which the express actions do not.[38] Consequently, it has become *the* most important weapon in combating securities fraud. *See supra*, Section II.B.1.

Applying a one year/three year period would prevent many defrauded investors from obtaining any relief under the federal securities laws. In many instances of fraud, such as Ponzi schemes, defaulted municipal bonds and other complex investment schemes, *see supra*, Section II.B.2., a plaintiff simply is not able to detect fraud within three years. A plaintiff's rights could be foreclosed even before fraud is discovered. A defendant need only set up a scheme that provides for some return for three years and wait for the period to expire. Applying a three year period of repose would have the effect of encouraging fraud and rewarding wrongdoers for successfully concealing their fraud. Section 10(b) would no longer function as a "catchall" antifraud mechanism, for it would not be able to deal with novel and

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[38] An action under § 10(b) "can be brought by a purchaser or seller of '*any* security' against '*any* person' who has used '*any* manipulative or deceptive device or contrivance'." *Herman & MacLean*, 459 U.S. at 382 (Court's emphasis). Because of the broad scope of these claims, there are many contexts in which the express federal actions and blue sky laws may not provide a remedy. The express terms of the statutes may provide only a limited remedy, or procedural restrictions may preclude class actions on other devices necessary when there are hundreds of defrauded investors. *See* Guin & Donaldson, *supra* note 10, at 572. Further, a § 10(b) claim can be brought against persons who manipulate securities prices, *see Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 303 (1985), the issuer of securities for false or misleading statements, *see Basic*, 485 U.S. 224, and against fiduciaries who trade in the securities market with material, non-public information, *see Dirks v. S.E.C.*, 463 U.S. 646, 653-54 (1983).

unforeseen methods of fraud.[39] Adopting a three year period of repose would reinstitute a philosophy of *caveat emptor*. Thus, it would undermine the remedial purposes of the Acts and conflict directly with the policy of encouraging private actions.

1. Congress Has Recently Indicated that Actions Involving Intentional Wrongdoing and Fraud Require a Longer Limitation Period than Three Years.

In § 20A of the Insider Trading Act, Congress provided a limitation period of "5 years after the date of the last transaction that is the subject of the violation." 15 U.S.C. § 78t-1(b)(4). This demonstrates Congress' awareness that the type of intentional wrongdoing involved in § 10(b) requires more than three years to bring an action.

The Interstate Land Sales Act, 15 U.S.C. §§ 1701 *et seq.* (1988), also demonstrates Congress' awareness that fraud often cannot be discovered within three years and requires a discovery-based limitation period that is not subject to a short

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[39] Fraud schemes are only becoming more subtle and ingenious:

> The newest twist – and the worst news for investors – is that investment frauds are claiming a wider range of victims. The cautious, conservative investor – generally immune to such things in the past – is becoming a prime target for con artists.
>
> Here's why. A decade of regulation in the securities industry has spawned crooks whose scams slither between the various laws – and remain out of the reach of regulators. In addition, financial bandits are targeting their victims with the same marketing savvy that Proctor & Gamble uses to sell soap. They're invoking God and country as they infiltrate every type of social group . . . and all financial advisory groups (including accountants & financial planners).

Schultz, Wall St. J., *supra* note 11, at p. R24, col.1.

period of repose.[40] The Interstate Land Sales Act was modeled after the Acts and has the same purpose of ensuring full disclosure and preventing fraud.[41] Section 1703(a)(2)(B-C) prohibits fraudulent practices in the land sales industry and is modeled after and virtually identical to Rule 10b-5.[42] But, unlike § 10(b) and Rule 10b-5, the Interstate Land Sales Act expressly provides for a private right of action. *See* 15 U.S.C. § 1709(a).

Congress initially provided a limitations period of "one year after the discovery of the untrue statement or the omission, or after such discovery should have been made . . . [but] [i]n no event . . . more than three years after the sale or lease. . . . " 15 U.S.C. § 1711 (1968). In 1979, Congress lengthened the limitations period to "three years after discovery of the violation or after discovery should have been made by the exercise of reasonable diligence." 15 U.S.C. § 1711(a)(2) (1988).[43] Congress lengthened the limitations

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[40] Congressional intent embodied in a statute with similar purposes is relevant. *See Capital Gains*, 375 U.S. at 186.

[41] *See United States v. Dacus*, 634 F.2d 441, 446 (9th Cir. 1980) (Interstate Land Sales Act originally "modeled on the Securities Act of 1933"); *Paquin v. Four Seasons of Tennessee, Inc.*, 519 F.2d 1105, 1109 (5th Cir. 1975), *cert. denied*, 425 U.S. 972 (1976) ("The Act closely parallels the philosophy and approach of the Securities Act of 1933. The underlying purpose of both is [to ensure full disclosure]"); *McCown v. Heidler*, 527 F.2d 204, 207 (10th Cir. 1975) (the general purpose of the Interstate Land Sales Act is "to prohibit and punish fraud" and should be construed broadly to effectuate its remedial purposes) (quoting *Capital Gains*, 375 U.S. at 195).

[42] Section 1703 is set forth in Appendix A. *See Gilbert v. Woods Marketing, Inc.*, 454 F.Supp. 745, 748 (D. Minn. 1978) (construing earlier version of § 1703(a)(2)(A-C) as "essentially similar to Rule 10b-5").

[43] At the same time, Congress amended § 1703 to more closely parallel Rule 10b-5. *See* H.R. Rep. No. 96-154, 96th Cong., 1st Sess. (1979), *reprinted in* 1979 U.S. Code Cong. & Admin. News 2317, 2350.

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period upon the realization that fraud often cannot be discovered within three years.[44] This is direct evidence of Congress' awareness that a three year period of repose is not appropriate for the type of conduct which § 10(b) addresses in light of the practical difficulty in discovering fraud. In short, in the two most recent instances where Congress has addressed fraud, it

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("The definition of a prohibited fraudulent activity is amended to conform more closely to the language found in the securities laws."). Further, Congress added prohibitions against making untrue statements or omissions in property reports or promotional material. *See* 15 U.S.C. § 1703(a)(1) (1988). Private actions for such misstatements must be brought within three years after signing the contract of sale or lease. 15 U.S.C. § 1711(a)(1). These added prohibitions are similar to §§ 11 and 12(2) of the 1933 Act. As with §§ 11 and 12(2), the relatively uncomplicated matter of identifying material misstatements or omissions in a property report is a fairly straightforward matter that can be discovered easily within three years.

[44] H.R. No. 96-154, *supra* note 43, at 2353-54:

> Statute of limitations problems have not been limited to purchasers paying installment contracts. Many purchasers buy land sight unseen, hold it for many years as an investment and never visit the property until they plan to retire. Only when they visit the property do they discover the promised roads have not been provided or maintained or the clubhouse has not been built or the land is uninhabitable because water is unavailable or the land is not suitable for septic tanks. Many such consumers have no remedy because the current statute of limitations in § 1412 [15 U.S.C. § 1711 (one year from discovery/three years from sale)] is unduly short. In fact, over 63% of the persons who complained to OILSR about land sales problems during a nine-month period in 1978 had no remedy because the statute of limitations had expired.
>
> * * *
>
> This bill would extend the statute of limitations affecting fraudulent sales . . . to three years after the discovery of the violation or after discovery should have been made by the exercise of reasonable diligence.

has chosen limitation periods that are *longer* than those provided in the express remedies of the Acts.

Congress' silence during the 45 years in which courts have implied a private right of action under § 10(b) (and applied state law) evidences Congress' acquiescence in this practice and in the expansive manner in which the courts have interpreted § 10(b).[45] In 1975, 1988 and 1990 Congress made significant amendments[46] to the Acts, yet it chose to leave intact the existing practice of borrowing state law for § 10(b). "In light of this well-established judicial interpretation, Congress' decision to leave Section 10(b) intact suggests that Congress ratified," the long-standing practice of applying state statutes of limitations. *Cf. Herman & MacLean*, 459 U.S. at 385-86; *see also Curran*, 456 U.S. at 381-82 ("the fact that a comprehensive reexamination and significant amendment of the CEA left intact the statutory provisions under which the federal courts had implied a cause of action is itself

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[45] Congress is presumed to be aware of the existing state of the law. *Merrill Lynch, Pierce, Fenner & Smith, Inc. v. Curran*, 456 U.S. 353, 379 (1982). Therefore, Congress is aware of judicial application and interpretation of § 10(b). *Cf.* H.R. Rep. No. 355, 98th Cong., 1st Sess. 3-4 (1983) *reprinted in* 3 Fed. Bar Ass'n Sec. L. Comm., *Federal Securities Law Legislative History 1933-1982*, Item 249, p. 4886-87 ("The Supreme Court has consistently construed [§ 10(b)] broadly"); *Agency Holding*, 483 U.S. at 147 (Congress is aware of the practice of borrowing state limitation periods).

[46] In 1975 Congress substantially revised the federal securities laws. *See Herman & MacLean*, 459 U.S. at 384-85 (discussing amendments of 1975). In 1988 Congress enacted the Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, 102 Stat. 4680 (codified at 15 U.S.C. § 78t-1), which added § 20A to the 1934 Act. In 1990 Congress enacted the Securities Enforcement Remedies & Penny Stock Reform Act of 1990, Pub.L. No. 101-429, 104 Stat. 931, the Market Reform Act of 1990, Pub.L. No. 101-432, 104 Stat. 963, and the Securities Acts Amendments of 1990, Pub.L. 101-550, 104 Stat. 2713.

evidence that Congress affirmatively intended to preserve that remedy").[47]

If Congress was dissatisfied with the practice of borrowing state law, it would have enacted a statute of limitations. *See Hoosier*, 383 U.S. at 704 ("when Congress has disagreed with such an interpretation of its silence, it has spoken to overturn it by enacting a uniform period of limitations"); *McLaughlin v. Richland Shoe Co.*, 486 U.S. 128, 131-32 (1988) (Congress rejected the practice of borrowing state law for civil actions under the Fair Labor Standards Act by enacting a statute of limitations); *Agency Holding*, 483 U.S. at 165-66 (Scalia, J., concurring) (if "Congress knows that we will borrow state statutes of limitations unless it directs otherwise, it also knows that it has to direct otherwise if it wants us to do something else").[48] Further, in enacting § 20A, Congress specifically stated that it did not wish to restrict the rights of action implied under the securities laws and wanted to give the courts the continued freedom to develop expansively such remedies. *See* H.R. Rep. No. 910, *supra* note 12, at 27.

2. The Goal of Uniformity Is Not a Sufficient Reason to Adopt a Three Year Period of Repose.

Petitioner's argument rests, principally, on the interests of achieving national uniformity.[49] However, the goal of

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[47] *See also Lorillard v. Pons*, 434 U.S. 575, 580-81 (1978) ("Congress is presumed to be aware of an administrative or judicial interpretation of a statute and to adopt that interpretation when it re-enacts a statute without change. . . . ") (*quoted in Curran*, 456 U.S. at 382 n.66).

[48] The Clayton Act, when originally enacted, did not contain an express statute of limitation for private actions. However, Congress later deemed that one was necessary and enacted one. *See* Clayton Act, Ch. 323, § 4B, 69 Stat. 283 (1955) (current version at 15 U.S.C. § 15b (1988)).

[49] Uniformity and certainty can be achieved, as it was in *Reed*, 488 U.S. 319, *Owens*, 448 U.S. 325, and *Wilson*, 471 U.S. 261, by uniform

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uniformity is not a sufficient reason in itself to institute a three year period of repose that would effectively undermine the policies behind § 10(b) and conflict with the practicalities of litigation. *Cf. Wilson*, 471 U.S. at 275 ("the need for national uniformity 'has not been held to warrant the displacement of state statutes of limitations for civil rights actions . . . ' ") (quoting *Board of Regents v. Tomanio*, 446 U.S. 478, 489 (1980)). Respondents do not contest that uniformity and repose[50] were policy considerations when Congress enacted the Acts. But focusing on the need for repose subverts the overall orientation and purpose of the Acts – to protect and provide relief to investors:

> the interests of defendants in a securities case do not differ qualitatively from the interests of defendants sued for violations of other federal statutes such as the antitrust or civil rights laws . . . [while] the interests of plaintiffs in such suits are significant. Defrauded investors are among the very individuals Congress sought to protect in the securities laws.

Herman & MacLean, 459 U.S. at 390.

If uniformity were an overriding policy, it would "warrant selection of a federal limitations period for almost any federal statute, a conclusion plainly inconsistent with the results of our cases." *Agency Holding*, 483 U.S. at 167

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characterization of the federal remedy to a single, state law cause of action. Thus, the concern for certainty and uniformity can be met by characterizing all § 10(b) private actions as analogous to common law fraud claims. *See supra* Section II.C.1.

[50] Congress' concern for repose was necessarily secondary to and dependant upon an assumption of how long it would reasonably take a plaintiff to discover a violation and bring an action. Since Congress and the SEC never even considered a private remedy under § 10(b), one cannot assume that the 73rd Congress had any awareness of how long it should take a plaintiff to bring such a claim. *See Blue Chip Stamps*, 421 U.S. at 737.

(Scalia, J., concurring). However, the settled rule is that "Congress intends by its silence that [courts] borrow state law," *id.* at 147, which necessarily presumes uniformity is not a paramount policy consideration.[51] If Congress thought this state of affairs severely hindered a plaintiff's ability to obtain relief under § 10(b), it would have long ago instituted a uniform limitations period.[52] *See Hoosier*, 383 U.S. at 704; *McLaughlin*, 486 U.S. at 131-32; *Agency Holding*, 483 U.S. at 165-66 (Scalia, J., concurring).

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[51] This Court has never stated that courts should reject state law in the interest of uniformity. *Agency Holding* considered "the desirability of a uniform federal statute of limitations," 483 U.S. at 154, but its analysis focused on whether state law was consistent with federal policy and practicalities of litigation. Further, civil RICO presented a unique situation: (1) it was modeled expressly after the Clayton Act; (2) unlike here, there were no remotely analogous state claims; (3) civil RICO can be analogized to a much larger universe of possible claims than § 10(b); and (4) applying state limitation periods directly conflicted with federal policies.

[52] Petitioner argues the current approach undermines "the effectiveness and value of § 10(b) as a remedy" because it leads to forum shopping and uncertainty as to the applicable limitations period. Pet.'s Br. at 28. But, Petitioner's purported solution would have the effect of preventing many plaintiffs from having any remedy at all. In § 313 of the recently enacted Judicial Improvements Act of 1990 ("JIA"), Pub. L. No. 101-650, 104 Stat. 5115, Congress enacted a uniform catchall statute of limitations period of "four years after the cause of action accrues." *See* Appendix A. However, it only applies *prospectively* to actions "arising under an Act of Congress enacted after the date of the enactment of this section. . . . " *Id.* Congress chose not to apply it to § 10(b) implied actions even though it was expressly suggested. *See* Staff of Federal Courts Study Comm., 101st Cong., 2d Sess., *Providing Federal Limitations Periods for all Federal Claims*. Thus, Congress has again deemed it unnecessary to apply a uniform federal statute of limitations to § 10(b) claims. Nonetheless, should this Court decide to look to federal law, rather than state law, § 313 offers an alternative limitation period that is better suited to § 10(b) actions than the one year/three year limitation periods.

The practical result of applying a one year/three year limitations period to private § 10(b) actions would only add uncertainty and inconsistency to § 10(b) litigation.[53] Plaintiffs who do not discover fraud and fail to bring a claim within three years will be denied relief under the federal securities laws. They will be forced into a variety of state or federal courts under blue sky and/or common law remedies. Cases of national fraud would be litigated at the same time in multiple state and federal forums.[54] This will only add to the forum shopping, uncertainty and inconsistency which Petitioner seeks to remedy and would defeat the purpose of the Acts to provide a uniform, national securities law to protect investors.

IV. SHOULD THIS COURT CHOOSE TO APPLY FEDERAL LAW, THE INTERSTATE LAND SALES ACT AND THE INSIDER TRADING ACT ARE MORE ANALOGOUS THAN THE EXPRESS REMEDIES.

A. The Interstate Land Sales Act.

The private right of action under the Interstate Land Sales Act, 15 U.S.C. § 1703(a)(2), is virtually identical in purpose and language to Rule 10b-5, and its limitation period of three years from constructive discovery, 15 U.S.C. § 1711(a)(2), is consistent with the practicalities of § 10(b)

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[53] In the context of federal securities litigation, the goal of uniformity is deceptive. No matter which limitation period is adopted, uniformity will not be achieved because of the constant potential for overlap between the many express actions of the original Acts and § 10(b). If a one year/three year period were adopted, a § 10(b) violation for stock market fraud could be subject to two different statutes of limitations – a one year/three year period or the five year period under § 20A. Creative lawyers could allege the claim as an insider trader violation. Further, there is still uncertainty as to *which* one year/three year period would apply. *See supra*, Section III.A.1.

[54] *See* Sontag, *supra* p. 28, at 24 ("If his clients lose their recourse under the federal securities laws, [an attorney] will refile the claims in numerous state courts.").

litigation. *See supra*, Section III.B.1. Therefore, it is sufficiently analogous to § 10(b) and is consistent with federal policy and practicalities of litigation. However, should the Court not adopt 15 U.S.C. § 1711(a)(2), Respondents agree with the SEC that § 20A provides a more appropriate solution than a three year period of repose.

B. Section 20A.

In enacting § 20A, 15 U.S.C. § 78t-1, Congress created an express remedy for insider trading, which is encompassed by § 10(b). Section 20A allows claims for violating the securities acts "by purchasing or selling a security while in possession of material, nonpublic information." 15 U.S.C. § 78t-1(a). Such actions must be brought within "5 years after the date of the last transaction that is the subject of the violation." 15 U.S.C. § 78t-1(b)(4).

As a particular type of Rule 10b-5 violation, a plaintiff must prove the same elements as for Rule 10b-5.[55] Further, the longer limitations period of five years better accommodates the remedial policies underlying § 10(b) and the practicalities of litigation. Nevertheless, § 20A is not clearly more analogous than state law and, thus, is not a better alternative than common law fraud statutes of limitations.

Section 20A explicitly applies to only a narrow type of wrongdoing. Congress specifically stated it did not want § 20A to be construed to limit the availability of any cause of action implied under the 1934 Act, 15 U.S.C. § 78t-1(d), and "wanted to give the courts leeway to develop such implied private rights of actions in an expansive fashion . . . ", H.R. Rep. No. 910, *supra* note 12, at 27. The five year limitations

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[55] However, § 20A requires that a defendant contemporaneously bought or sold the same class of stock as did the plaintiff. 15 U.S.C. § 78t-1(a).

period applies only to actions "brought under this section." 15 U.S.C. § 78t-1(b)(4).[56] Therefore, Congress made it as clear as possible that the five year period should not apply to § 10(b) claims beyond the scope of § 20A.

Section 20A also suffers from the same problems as the other express actions. Its limitations period is not discovery-based. A claim may be barred even if a plaintiff has failed, in the exercise of reasonable diligence, to detect fraud.[57] Accordingly, § 20A, as with the other express remedies, is not broad enough to be sufficiently analogous to § 10(b) claims. It would conflict with the remedial policy of the Acts and does not accommodate the practicalities of § 10(b) litigation. Common law fraud, on the other hand, provides the closest analogy and, by applying the *Wilson* approach, would best promote federal policy and accommodate the practicalities of litigation while achieving a necessary degree of uniformity and certainty.

V. FEDERAL POLICY REQUIRES THAT ANY SECTION 10(b) STATUTE OF LIMITATIONS BE TOLLED FOR DILIGENT PLAINTIFFS WHO HAVE NOT DISCOVERED FRAUD OR WHERE DEFENDANTS HAVE ACTIVELY CONCEALED THE FRAUD.

The doctrine of equitable tolling "is read into every federal statute of limitation." *Holmberg*, 327 U.S. at 397. Federal courts uniformly toll state statutes of limitations in § 10(b) cases where reasonably diligent plaintiffs are unaware of their claims through no fault of their own, or where

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[56] *See also* H.R. Rep. No. 355, *supra* note 45, at 12 ("The limitations period [of five years] is applicable solely to actions brought under this legislation.").

[57] However, as with the other express actions, insider trading does not go long unnoticed due to the degree to which the national exchanges are watched. *See* H.R. Rep. No. 355, *supra* note 45, at 30 ("in most instances, insider trading is discovered, if at all, soon after it occurs.").

defendants have actively concealed the fraud.[58] This Court has held that fraud statutes of limitations must be tolled under these circumstances[59]:

> To hold that by concealing a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statute of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure. And we see no reason why this principle should not be as applicable to suits tried on the common law side of the court's calendar as to those on the equity side.

Bailey v. Glover, 88 U.S. (21 Wall.) 342, 349 (1874).

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[58] *See, e.g., Volk v. D.A. Davidson & Co.*, 816 F.2d 1406, 1415 (9th Cir. 1987); *Cook*, 573 F.2d 685. Federal law governs when the claim accrues even where an applicable state blue sky law statute of limitations contains a statute of repose. *Hudak v. Economic Research Analysis*, 499 F.2d 996, 1000 (5th Cir. 1974) (fraudulent concealment tolls Florida blue sky statute of repose). Ever since a right of action was implied under § 10(b), Congress has acquiesced to judicial development of § 10(b) cases, including the doctrines of equitable tolling and fraudulent concealment without expressing any concern that plaintiffs' right to a remedy was being unduly promoted over defendants' interest in repose.

[59] *See Bailey v. Glover*, 88 U.S. (21 Wall.) 342 (1874); *Exploration Co. v. United States*, 247 U.S. 435 (1918); *Holmberg*, 327 U.S. 392; *American Pipe & Constr. Co. v. Utah*, 414 U.S. 538 (1974). The doctrine of equitable tolling also applies to the Clayton Antitrust Act, the Reconstruction Era Civil Rights Acts, the Commodity Exchange Act, the Federal Tort Claims Act, the National Labor Relations Act, the Railway Labor Act, the Death on the High Seas Act, the Interstate Land Sales Full Disclosure Act, the Omnibus Crime Control and Safe Streets Act of 1968, the Age Discrimination and Employment Act, the Emergency Petroleum Allocation Act, the Occupational Safety and Health Act of 1970, the Motor Vehicle Information and Cost Savings Act, the Employee Retirement Income Security Act, the Selective Service Act, the Copyright Act, claims against the United States under the Tucker Act, suits to recover taxes and cases involving claims based on the Constitution. *See* R. L. Marcus, *Fraudulent Concealment in Federal Court: Toward a More Disparate Standard?* 71 Georgetown L.J. 801, 831-33 (1983) (and cases cited therein).

In *Holmberg*, this Court again affirmed the importance of applying the federal tolling doctrine to claims involving fraud:

> [W]here a plaintiff has been injured by fraud and "remains in ignorance of it without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, though there be no special circumstances or efforts on the part of the party committing the fraud to conceal it from the knowledge of the other party." *Bailey v. Glover*, 21 Wall. 342, 348; and *see Exploration Co. v. United States*, 247 U.S. 435; *Sherwood v. Sutton*, 5 Mason 143.

327 U.S. at 397.

Most recently, the Federal Courts Study Committee concluded that even though there should be a uniform, catchall statute of limitations, the fraudulent concealment doctrine should be retained because a short statute of repose produces unfair results:

> The committee does *not* recommend abandoning the sometimes troublesome fraudulent concealment doctrine, which plaintiffs can use to argue for effective extension of the limitations period. Fairness argues against rewarding wrongdoers who succeed in concealing their misdeeds long enough, and the difficulties of making out a case of fraudulent concealment protect against widespread abuse of the doctrine.

Report of the Federal Courts Study Committee[60] ("Fed. Cts. Rpt.") (April 2, 1990) pp. 93-94. Not only is there long

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[60] In 1988, Congress created a Federal Courts Study Committee which was directed to make a complete study of the courts of the United

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established precedent for the application of the doctrines of equitable tolling and fraudulent concealment to fraud claims, but there is also recent congressional awareness of the importance of these doctrines. Therefore, these doctrines should be applied to any new statute of limitations applied to § 10(b) actions.

VI. ANY CHANGE IN THE LAW SHOULD BE APPLIED PROSPECTIVELY ONLY.[61]

In *Chevron Oil Co. v. Huson*, 404 U.S. 97 (1971), this Court outlined three factors to consider to determine whether to apply a new rule of law retroactively or prospectively.

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States. Fed. Cts. Rpt. p. 31. In the Report, the Committee recommended the adoption of a catchall, uniform limitations period for all federal causes of action, express or implied, that presently lack statutes of limitations. *Id.*, p. 93. Apparently, on the basis of this recommendation, Congress enacted § 313 of the JIA which provides a limitation period of "4 years after the cause of action accrues." Pub. L. No. 101-650, 104 Stat. 5115. However, it applies only prospectively to causes of action arising under later enacted statutes. This demonstrates congressional intent that, generally, any new uniform statute of limitations should apply prospectively.

[61] Petitioner and Respondents Comdisco and Pontikes do not address this issue but apparently assume any new rule will apply retroactively. *Amicus* American Council of Life Insurance argues that any new rule should be applied to cases filed after September 22, 1987 (*Amicus* American Council's Br. at 13 n.5), based upon the date of *Agency Holding*, 483 U.S. 143. The Third Circuit categorically rejected this argument in *Gruber v. Price Waterhouse*, 911 F.2d 960, 967 (3d Cir. 1990). This would not affect this case as the original complaints were filed on November 3, 1986 in the *Gilbertson* and *Reitz* lawsuits, and on June 4, 1987, in the *Catalan* lawsuit. *Amici* Arthur Andersen, et al., take the position that the issue should first be determined by the lower courts on remand. *Amici* Arthur Andersen & Co., et al.'s Br. at 29 n.16. This would, of course, result in years of further litigation on issues such as whether plaintiffs relied on any overruled precedent. The inquiry could be different in each circuit, varying according to the established precedent and facts of the case.

First, does the new decision overrule "clear past precedent on which litigants may have relied" or decide "an issue of first impression whose resolution was not clearly foreshadowed"? *Id.* at 106-7. Second, a court must consider the "merits and demerits" of the case "by looking to the prior history of the rule in question, its purpose and effect, and whether retrospective operation will further or retard its operation." *Id.* (internal quotation omitted). Third, would retroactive application "produce substantial inequitable results"? *Id.* at 107. Further, courts should not indulge in the fiction that the new rule always has been the law. *Id.* Applying these factors, a new uniform statute of limitations for § 10(b) cases should only be applied prospectively.[62]

A. A New Statute of Limitations Would Establish a New Principle of Law and Overrule Clear Past Precedent in the Ninth Circuit.

In the Ninth Circuit, the long established rule has been to borrow the forum state's statute of limitations for fraud.[63] If the Court adopts a new uniform statute of limitations, it will "effectively [overturn] a long line of decisions" and clear precedent within the Ninth Circuit. *See Huson*, 404 U.S. at

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[62] This Court also has acknowledged that a new statute of limitations must allow a reasonable time after taking effect for existing causes of action to be commenced, a rule that has constitutional implications. *Wilson v. Iseminger*, 185 U.S. 55, 62 (1902); *Brinkerhoff-Faris Trust & Savings Co. v. Hill*, 281 U.S. 673, 681-82 (1930).

[63] *See, e.g., Volk*, 816 F.2d at 1412 (applying Montana's fraud statute of limitation); *Semegen v. Weidner*, 780 F.2d 727, 733 (9th Cir. 1985); *Admiralty Fund v. Hugh Johnson & Co.*, 677 F.2d 1301, 1308-09 (9th Cir. 1982); *Williams v. Sinclair*, 529 F.2d 1383, 1387 (9th Cir. 1975) (applying Oregon's fraud statute of limitation); *Douglass v. Glenn E. Hinton Invs., Inc.*, 440 F.2d 912, 915-16 (9th Cir. 1971) (applying Washington's fraud statute of limitation).

107. Thus, the first *Huson* factor strongly supports prospective application of a new statute of limitations.[64]

B. Retroactive Application of a New Statute of Limitations Would Neither Further nor Retard its Application.

The second *Huson* factor requires a court to weigh the merits and demerits of the case "to determine the scope of the rule and to ascertain whether [its] retroactive operation would further or retard the rule." *Gruber v. Price Waterhouse*, 911 F.2d 960, 967 (3d Cir. 1990) (refusing to apply *Data Access* rule retroactively).

This component is neutral under the circumstances of a § 10(b) case. Even though uniformity in pending litigation would be promoted by simply applying a new statute of limitation retroactively, the " 'reasoning swallows the rule.' " *Id.* at 968. All pending § 10(b) cases, notwithstanding their merits, would be subject to possible dismissal even when the plaintiffs have relied on clear precedent, or would involve

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[64] *See St. Francis College v. Al-Khazraji*, 481 U.S. 604, 608 (1987) (new statute of limitations applied prospectively because it overruled clearly established precedent on which party was entitled to rely and because retroactive application would be inconsistent with purpose of underlying statute and manifestly inequitable); *Kelly v. Burlington Northern R. Co.*, 896 F.2d 1194, 1199 (9th Cir. 1990) (either old rule applies or new rule applies and begins to run from date new rule is imposed); *Smith v. Firestone Tire and Rubber Co.*, 875 F.2d 1325, 1327 (7th Cir. 1989) (same); *Pucci v. Santi*, 711 F.Supp. 916 (N.D.Ill. 1989) (when new statute of repose is imposed, it begins to run on the date of the new rule); *see also Sohn v. Waterson*, 84 U.S. (17 Wall.) 596 (1873) (if statute imposes statute of limitations where none previously existed, it begins to run on effective date). When new statutes of repose have been applied in the medical malpractice area, courts or state legislatures have applied them prospectively only to prevent unfairness. *See Moore v. Jackson Park Hospital*, 447 N.E.2d 408, 413-14 (Ill. 1983) and cases and statutes cited therein.

extensive litigation of that issue. This Court, like the Third Circuit in *Gruber*, should be "compelled to conclude that the second factor 'does not "militate clearly either in favor of or against retroactive application" and is therefore neutral.' " *Id.* (citations omitted).

C. Retroactive Application of a New Statute of Limitations Would Produce Substantial Inequitable Results.

In this case, retroactive application of a new rule would produce substantial, inequitable results. Respondents' § 10(b) claims would not be barred but for the imposition of a new statute of limitations created more than four years after these cases were commenced. *See Huson*, 404 U.S. at 108; *Gruber*, 911 F.2d at 968; *In re Nat'l Smelting of New Jersey, Inc., Bondholders Litig.*, 722 F.Supp. 152, 160 (D.N.J. 1989). At the time these cases were commenced, the clearly established law in the Ninth Circuit was to look to the state statute of limitation for fraud. *See, e.g., Volk*, 816 F.2d 1406. It would be inequitable to conclude that plaintiffs "slept on their rights" and thus are deprived of their day in court when the rules changed after they invested and filed suit.[65]

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[65] Defendants also should not be allowed to argue that since plaintiffs did not discover their claims within three years of investing, they are not harmed by their reliance on the old rule because they would never have been able to file a timely case under a three year statute of repose. Defendants consistently had taken the opposite position. They repeatedly have argued that plaintiffs were on inquiry or actual notice of fraud quite early because the investments were not economic successes. Pet.'s Cert. Br. at 34A. Plaintiffs contend otherwise, but acknowledge that, within three years of investing, there was information the investments were economically unsuccessful although insufficient to place plaintiffs on notice of possible fraud. The Ninth Circuit agreed. Thus, defendants cannot now argue that plaintiffs could not have relied upon established Ninth Circuit precedent when they did not investigate

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CONCLUSION

Section 10(b) should not be restricted by the unduly short one year/three year statute of limitations of the express private remedies of the 1933 and 1934 Acts. Applying a three year period of repose that is not discovery-based will prevent many investors from obtaining any relief under the Acts for securities fraud. The elements and scope of § 10(b) actions, let alone their existence, go far beyond what Congress envisioned when it fashioned the one year/three year limitations period for the express remedies. The policies furthered by § 10(b) and the practicalities of litigation mandate that § 10(b) not be subject to a three year period of repose.

Common law fraud statutes of limitation provide an appropriate choice for § 10(b) actions. The similarity of their elements and purpose in addressing fraud makes those statutes sufficiently analogous to § 10(b). Uniform application of such statutes would further the remedial policies of the federal securities laws and accommodate the practicalities of litigation, while addressing concerns for uniformity and certainty.

(Continued from previous page)

for fraud upon learning of the lack of success of their investments. This is something all investors will have to do if the Court adopts an absolute three year statute of repose, even though there is no indication of fraud. *Pucci* forcibly points out the distinction between a new statute of limitations and a new statute of repose in a fraud situation – a statute of limitations requires due diligence, but a statute of repose requires *extraordinary* diligence. 711 F.Supp. at 924. *Cf. Firestone Tire and Rubber Co.*, 875 F.2d at 1327 (inequity in retroactive application of *shorter* limitations period than previously applied is a factor to be considered).

For the reasons above, the Court of Appeals should be affirmed.

Respectfully submitted,

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APPENDIX

SECTION 1404(a) OF THE INTERSTATE LAND SALES FULL DISCLOSURE ACT, 15 U.S.C. § 1703(a):

§ 1703. Requirements respecting sale or lease of lots

(a) Prohibited activities. It shall be unlawful for any developer or agent, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce, or of the mails –

(1) with respect to the sale or lease of any lot not exempt under section 1403 [15 U.S.C. § 1702] –

(A) to sell or lease any lot unless a statement of record with respect to such lot is in effect in accordance with section 1407 [15 U.S.C. § 1706];

(B) to sell or lease any lot unless a printed property report, meeting the requirements of section 1408 [15 U.S.C. § 1707], has been furnished to the purchaser or lessee in advance of the signing of any contract or agreement by such purchaser or lessee;

(C) to sell or lease any lot where any part of the statement of record or the property report contained an untrue statement of a material fact or omitted to state a material fact required to be stated therein pursuant to sections 1405 through 1408 of this title [15 U.S.C. §§ 1704 through 1707] or any regulations thereunder; or

(D) to display or deliver to prospective purchasers or lessees advertising and promotional material which is inconsistent with information required to be disclosed in the property report; or

(2) with respect to the sale or lease, or offer to sell or lease, any lot not exempt under section 1403(a) [15 U.S.C. § 1702(a)] –

(A) to employ any device, scheme, or artifice to defraud;

(B) to obtain money or property by means of any untrue statement of a material fact, or any omission to state a material fact necessary in order to make the statements made (in light of the circumstances in which they were made and within the context of the overall offer and sale or lease) not misleading, with respect to any information pertinent to the lot or subdivision;

(C) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon a purchaser; or

(D) to represent that roads, sewers, water, gas, or electric service, or recreational amenities will be provided or completed by the developer without stipulating in the contract of sale or lease that such services or amenities will be provided or completed.

* * *

SECTION 1410(a), (b) OF THE INTERSTATE LAND SALES FULL DISCLOSURE ACT, 15 U.S.C. § 1709(a), (b):

§ 1709. Civil liabilities

(a) Violations; relief recoverable. A purchaser or lessee may bring an action at law or in equity against a developer or agent if the sale or lease was made in violation of section 1404(a) [15 U.S.C. § 1703(a)]. In a suit authorized by this subsection, the court may order damages, specific performance, or such other relief as the court deems fair, just, and equitable. In determining such relief the court

may take into account, but not be limited to, the following factors: the contract price of the lot or leasehold; the amount the purchaser or lessee actually paid; the cost of any improvements to the lot; the fair market value of the lot or leasehold at the time relief is determined; and the fair market value of the lot or leasehold at the time such lot was purchased or leased.

(b) Enforcement of rights by purchaser or lessee. A purchaser or lessee may bring an action at law or in equity against the seller or lessor (or successor thereof) to enforce any right under subsection (b), (c), (d), or (e) of section 1404 [15 U.S.C. § 1703(b), (c), (d), or (e)].

* * *

SECTION 1412 OF THE INTERSTATE LAND SALES FULL DISCLOSURE ACT, 15 U.S.C. § 1711(a):

§ 1711. Limitation of actions

(a) No action shall be maintained under section 1410 [15 U.S.C. § 1709] with respect to –

(1) a violation of subsection (a)(1) or (a)(2)(D) of section 1404 [15 U.S.C. § 1703(a)(1) or (a)(2)(D)] more than three years after the date of signing of the contract of sale or lease; or

(2) a violation of subsection (a)(2)(A), (a)(2)(B), or (a)(2)(C) of section 1404 [15 U.S.C. § 1703(a)(2)(A), (a)(2)(B), or (a)(2)(C)] more than three years after discovery of the violation or after discovery should have been made by the exercise of reasonable diligence.

* * *

SECTION 313 OF THE JUDICIAL IMPROVEMENTS ACT OF 1990, Pub.L. No. 101-650, 104 Stat 5115:

> Except as otherwise provided by law, a civil action arising under an Act of Congress enacted after the date of the enactment of this section may not be commenced later than 4 years after the cause of action accrues.

Supreme Court, U.S.
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No. 90-333

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, JOHN V. REITZ, and ANTHONY CATALAN, *et al.*,
Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

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REPLY BRIEF FOR PETITIONER

Respondents' Brief contains fundamental errors in law and in logic, as well as irreconcilable internal inconsistences, that eviscerate the arguments they advance in this case.

A. The Intentions of the Congress that Enacted § 10(b) are Directly Relevant to the Choice of a Limitations Period for Private Actions Brought Pursuant to that Section.

Respondents and *amicus curiae* Securities and Exchange Commission ("Commission") misapprehend this Court's function in conducting interstitial lawmaking with respect to the contours of a federally created right. To ascertain a limitations period for a private remedy created expressly or by implication by Congress, the Court must discern, as faithfully as possible, "the balance that *Congress would have preferred* between the substantive policies underlying the federal claim and the policies of repose." *Wilson* v. *Garcia*, 471 U.S. 261, 270 (1985) (emphasis added).[1] Yet respondents and the Commission urge the Court to look everywhere but at the single most pertinent source of information regarding what Congress "would have preferred" as a limitations period for private actions under § 10(b) at the time it enacted that provision. *See, e.g.*, Br. for Resp. at 6, 31 n.37; Br. for SEC at 9 n.13.

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[1] In *DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151 (1983), the Court described its methodology as discerning what "Congress would likely intend," *id.*, at 158-59 n.12, or what "Congress would choose to adopt," *id.*, at 161. In *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), the Court focused its attention on the "clear legislative intent" to pattern the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1961, *et seq.*, on the Clayton Act as a rationale for borrowing the latter's four-year statute of limitations for RICO cases, *id.*, at 152, and rejected a Pennsylvania limitations period because it "was unlikely that Congress would have intended such a statute of limitations to apply," *id.*, at 153.

On the one hand, respondents (and the Commission) perceive congressional intent as irrelevant in determining the confines of private remedies under § 10(b). They therefore brush aside the motivation, debate, and ultimate policy judgments of the Congress whose actions created both the remedy under § 10(b) and the carefully crafted, comprehensive federal regulatory scheme of which it is an integral part. *See* Br. for Pet. at 11-15. That Congress, with the benefit of intense public comment and thorough debate, balanced the rights of victims of alleged securities fraud against the need for stability and certainty in the Nation's capital markets, and repeatedly determined that securities fraud actions under federal law should be governed by one-year/three-year limitations and repose periods.[2] Respondents argue that this compelling evidence of what Congress "would have preferred" is irrelevant and summarily reject it in a footnote. Br. for Resp. at 31 n.37.

On the other hand, respondents are captivated by evidence of legislative intent that they divine from congressional inaction, silence and omissions occurring decades after § 10(b) was enacted. Their school of statutory construction might be christened "inaction speaks louder than words." Thus, respondents argue (a) that "Congress intends *by its silence* that courts should apply state law" (Br. for Resp. at 6) (emphasis added); (b) that congressional failure to reverse judicial application of state limitations periods constitutes "ratification" of this practice (Br. for Resp. at 7, 36-37); (c) that amendments in 1979 to laws governing the sale of real estate, having nothing whatever to do with securities or § 10(b), furnish "direct evidence" that Congress is aware that a "three year period of repose is not appropriate" for § 10(b) cases (Br. for Resp. at 35); (d) that a congressional decision in 1990 *not* to include § 10(b) actions in a new federal statute of limitations constitutes evidence that Congress does not want a "uniform federal statute of limitations [for] § 10(b) claims"

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[2] *See* Bloomenthal, *Statutes of Limitations and the Securities Acts—Part I*, 7 Sec. & Fed. Corp. L. Rep. 17, 20 & nn. 30-31 (Mar. 1985).

(Br. for Resp. at 39 n.52); (e) that in 1988, when Congress enacted § 20A of the Insider Trading and Securities Fraud Enforcement Act and explicitly provided that it did *not* want the new law to affect other rights of action under the securities laws, it thereby signaled that it "wanted to give the courts the continued freedom to develop expansively such remedies" (Br. for Resp. at 37); and (f) that congressional enactment of a new statute of limitations in 1990 that does not apply to § 10(b) "demonstrates congressional intent that . . . any new uniform statute of limitations should apply prospectively." (Br. for Resp. at 45 n.60).

In short, respondents have produced a remarkable *tour de force* that turns traditional canons of statutory construction inside out. Legislative intent is irrelevant to respondents and reference to it is "inherently misguided" (Br. for Resp. at 31 n.37) when it pertains to the Congress that created the 1933 and 1934 securities acts and § 10(b), but becomes highly persuasive when Congress does nothing or considers unrelated matters decades later. Respondents ignore Congress when it does speak and pay attention when it does not.

As the Court has explained, "[l]egislative silence is a poor beacon to follow in discerning the proper statutory route." *Zuber* v. *Allen*, 396 U.S. 168, 185 (1969). Indeed, " '[i]t is at best treacherous to find in congressional silence alone the adoption of a controlling rule of law'." *Id.*, at 185-86 n.21 (quoting *Girouard* v. *United States*, 328 U.S. 61, 69 (1946)); *see, e.g.*, *Patterson* v. *McLean Credit Union*, 109 S. Ct. 2363, 2372 n.1 (1989); *Aaron* v. *SEC*, 446 U.S. 680, 693-94 n.11 (1980) (because "significant amendments to the securities laws" were "addressed principally to matters other than that at issue here, it is our view that the failure of Congress to overturn the Commission's interpretation falls far short of providing a basis to support a construction of § 10(b) so clearly at odds with its plain meaning and legislative history"). In *Agency Holding Corp.*, the Court established a uniform federal limitations period for civil RICO actions despite congressional failure to set

aside the decisions of several courts applying various state limitations periods to such claims and notwithstanding congressional actions or inactions similar to those cited by respondents here. *See* 483 U.S., at 154-55.

It would indeed be anomalous to attribute to Congress an intention to apply inconsistent state limitations periods to a federal right of action "found by the courts to be implied in a general statutory scheme—especially when that general statutory scheme itself contains a federal statute of limitations for a related but separate form of relief." *DelCostello*, 462 U.S., at 159 n.12; *see also United Parcel Service, Inc.* v. *Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring in the judgment) ("it cannot reasonably be assumed . . . that congressional silence reflects an intent to apply state statutes of limitation for an [implied] action . . . traceable to [a statutory scheme that includes an express limitations period]"). Here, as in *DelCostello*, the general statutory scheme, *i.e.*, the 1933 and 1934 Acts, and their language, structure and legislative history, leave no room for such an incongruous assumption. The Seventy-Third Congress repeatedly balanced the competing equities between private securities fraud actions under federal law and the interests of repose and repeatedly made the identical choice: a one-year/three-year limitations period.[3] *See Agency Holding Corp.*, 483 U.S., at 156.

In defining the scope of the § 10(b) implied private action, this Court has consistently remained faithful to the intent of the Seventy-Third Congress.[4] *See, e.g., Blue Chip*

[3] Respondents (Br. for Resp. at 29) and the Commission (Br. for SEC at 21) make the point that there are some distinctions in the phrasing of the various 1933 and 1934 Act one-year/three-year limitations periods. However, such differences are trivial, especially when compared with the wide disparity between the one, two, three, four, five and six year state limitations periods under respondents' suggested formula, *see infra* page 11, and any potential confusion can easily be eliminated by the Court's endorsement, as petitioner has suggested, of the specific limitations period set out by Congress for § 9 of the 1934 Act.

[4] This approach is consistent with the Court's conclusion that inferring a private right of action under federal law depends ultimately on whether "Congress intended to create a private cause of action." *Karahalios* v. *National Federation of Federal Employees*, 489 U.S. 527, 532 (1989); *see also Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 568 (1979). It makes no sense to examine congressional intent to see whether such a right exists and not consult the same sources to determine the breadth and limitations of such a right.

Stamps v. *Manor Drug Stores*, 421 U.S. 723, 733-36 (1975) (examining language and structure of the 1933 and 1934 Acts to determine whether the § 10(b) remedy is limited to purchasers and sellers of securities); *see id.*, at 755-61 (Powell, J., concurring) ("emphasiz[ing] the significance of the texts of the Acts of 1933 and 1934" in discerning the intent of Congress with respect to the meaning of § 10(b)); *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 214 (1976) (a requirement of scienter under § 10(b) "was compelled by the language and history of § 10(b) and related sections of the [1933 and 1934] Acts"); *see also Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 473 (1977). And the Court has emphasized "Congress' intent in adopting other portions of the Securities Exchange Act when [it] endeavor[s] to discern the limits of private causes of action under Rule 10b-5." *Basic Inc.* v. *Levinson*, 485 U.S. 224, 257 (1988) (White, J., concurring in part and dissenting in part) (citing *Ernst & Ernst*, 425 U.S., at 204-06).[5] Respondents offer no justification for departing from that practice in this case.

B. The One-Year/Three-Year Rule is Clearly the Most Appropriate Limitations Period for § 10(b) Private Actions.

Respondents and the Commission do not address the close textual, structural and purposive relationship be-

[5] The Court has been particularly careful to avoid constructions of § 10(b) that would expand the scope of its "implied cause of action beyond the bounds [Congress] delineated for comparable express causes of action." *Blue Chip Stamps*, 421 U.S., at 736; *see also Touche Ross & Co.*, 442 U.S., at 574 ("we are extremely reluctant to imply a cause of action . . . that is significantly broader than the [principal express civil] remedy"); *Miles* v. *Apex Marine Corp.*, 111 S. Ct. 317, 326 (1990) ("[i]t would be inconsistent with our place in the constitutional scheme were we to sanction more expansive remedies in a judicially-created cause of action . . . than Congress has allowed in [express actions]").

tween § 10(b) and the express rights of action created at the same time. *See* Br. for Pet. at 11-15, 32-42. Instead, they examine independently the elements of each of the express rights of action, discover, not surprisingly, that each differs in some respect from § 10(b) and leap to the *non sequitur* that the broad right created by § 10(b) must have a different limitations period than the other species of securities fraud created by the Seventy-Third Congress. But it simply transcends logic to conclude that the Seventy-Third Congress would have intended that any private remedy for the conduct it prohibited in 1933 and 1934 be subject to fifty different state limitations periods rather than the one standard it repeatedly endorsed.

For example, respondents identify "the requirement of scienter" as "the distinguishing feature of § 10(b) litigation" (Br. for Resp. at 15), and argue that it would be "draconian" to impose a one-year/three-year limitations period in light of § 10(b)'s scienter requirement, *see* Br. for Resp. at 21 n.19. However, the requirement of scienter is not unique to the § 10(b) implied right of action. A private plaintiff under § 9 of the 1934 Act, which prohibits "willful" manipulation of securities prices, must also prove scienter to prevail. *See Ernst & Ernst*, 425 U.S., at 205; *see also* Br. for SEC at 19 n.27 (§ 9 "requires proof of scienter"); 1 A. Bromberg & L. Lowenfels, *Securities Fraud & Commodities Fraud* § 2.4, at 2:207 (Supp. 1989) ("§ 9 is full of scienter"). Indeed, the Court's conclusion in *Ernst & Ernst* that the § 10(b) right of action includes a scienter requirement was predicated in substantial part upon the close substantive and historical relationship between §§ 9 and 10(b). *See* 425 U.S., at 201-05.[6]

[6] That relationship refutes the speculation of respondents and the Commission that Congress enacted the one-year/three-year limitations period because of the "comparatively light burden placed on a plaintiff in an action under many of the express provisions." Br. for SEC at 19; Br. for Resp. at 28. The only legislative history cited to support this argument is one Senator's comment that, in some private actions subject to the one-year/three-year rule, "the burden of proof is shifted around on the question of knowledge or willfulness in a misrepresentation." 78 Cong. Rec. 8201 (May 7, 1934) (statement of Sen. Austin). However that statement was a reference to § 18 of the 1934 Act, 15 U.S.C. § 78r, which permits a defendant to avoid liability by proving good faith and lack of knowledge that a statement was false or misleading. *See Ernst & Ernst*, 425 U.S. at 211 n.31 (describing § 18 liability). It does not pertain to § 9, which imposes impediments to recovery that are at least as rigorous as § 10(b)'s. In fact, "[p]roof requirements appear much easier under 10b-5 than under [§ 9] for market manipulation." 1 A. Bromberg & L. Lowenfels, *supra*, § 2.5(4), at 44.2; *see also* Br. for Resp. at 27 n.29 ("§ 9(e) has a strict causation requirement which is difficult for plaintiffs to satisfy"); L. Loss, *Fundamentals of Securities Regulation* 920-21 (2d ed. 1988) (describing difficulties of proving a § 9 violation and concluding that § 9 is "no bargain" for plaintiffs).

Respondents (Br. for Resp. at 27) and the Commission (Br. for SEC at 19 n.27) also urge the Court to reject § 9(e)'s statute of limitations because § 9 has been a less popular vehicle for securities fraud litigation than § 10(b). But that contention proves too much, and, in fact, illustrates why the Court should adopt for § 10(b) actions the express limitations enacted by Congress rather than judicially repealing those provisions by adopting a longer limitations period for § 10(b).

In 1941, prior to the judicial recognition of an implied right of action under § 10(b), the Commission itself referred to § 9 as "the very heart of the [Exchange Act]" and, indeed, the "most important safeguard afforded [to investors] by the act." *Report of the Securities and Exchange Commission on Proposals for Amendments to the Securities Act of 1933 and the Securities Exchange Act of 1934* 50 (Aug. 7, 1941). Shortly thereafter, a private right of action was inferred from § 10(b).[7] The courts soon began to permit, and in some respects eased, recovery under § 10(b) for fraudulent and manipulative conduct expressly prohibited by § 9,[8] and incorporated § 9 by reference in § 10(b) cases involving securities not registered on a na-

[7] *See Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946).

[8] *See, e.g., Chemetron Corp.* v. *Business Funds, Inc.*, 718 F.2d 725, 729-30 (5th Cir. 1983), (holding that § 10(b) permits actions for manipulation of securities prices without proof that manipulation "affected" price as required by § 9(a)).

tional exchange.[9] The implied remedy has thus tended to eclipse the express one.

Because many of the express actions can artfully be pleaded as § 10(b) claims, adopting a limitations period for § 10(b) claims that is longer than the express limitations period prescribed by Congress for § 9 and the other express remedies would therefore nullify the explicit decisions by Congress to limit the time within which the express actions may be maintained—an outcome that the Court should surely strive to avoid.[10]

The Commission contends that application of a one-year/three-year limitations period to § 10(b) claims is inappropriate because § 10(b) has "come to embrace a diversity of claims which could not have been envisioned in 1934." Br. for SEC at 23; *see also* Br. for Resp. at 32-33. But Congress not only anticipated but intended that § 10(b) would function as a "catchall" to encompass fraudulent conduct not specifically prohibited by the express remedies of the 1933 and 1934 Acts. *See Ernst & Ernst*, 425 U.S., at 203. Moreover, even if § 10(b)'s ambit has been expanded by the courts, that does not warrant the materially greater judicial expansion that would result if § 10(b) claims

[9] *See, e.g., Edward J. Maywod & Co.* v. *SEC*, 591 F.2d 588, 595 (10th Cir. 1979). The Commission emphasizes the fact that § 9, unlike § 10(b), applies "exclusively to securities registered on a national securities exchange," Br. for SEC at 18-19, as a justification for applying the one-year/three-year period to § 9, but not to § 10(b). That is a difference but not a distinction. Congress adopted a one-year/three-year limitations period for §§ 11 and 12 of the 1933 Act, 15 U.S.C. § 77k, 77*l*, and § 29(b) of the 1934 Act, 15 U.S.C. § 78cc, none of which is limited in application to exchange-traded securities.

[10] *See Ernst & Ernst*, 425 U.S., at 210; *Blue Chip Stamps*, 421 U.S., at 735-37; *see also McAllister* v. *Magnolia Petroleum Co.*, 357 U.S. 221, 225-26 (1958) (applying express Jones Act statute of limitations to related admiralty claims to avoid frustrating Congress' intent with respect to the Jones Act limitations period); *Piper* v. *Chris-Craft Industries, Inc.*, 430 U.S. 1, 45-46 (1977) (referring to "the close relationship of Rule 10b-6 with § 9" and precluding a Rule 10b-6 claim that did not seek recovery for the kind of losses contemplated by § 9).

are subjected to a longer statute of limitations than the express remedies thoughtfully crafted and carefully limited by Congress. To the contrary, the need for predictability and repose, which prompted Congress to adopt the one-year/three-year rule, is even greater in the context of a broadly worded, open-ended antifraud provision such as § 10(b).[11]

Although the various express rights of action of the 1933 and 1934 Acts target separate categories of fraudulent conduct and impose different substantive burdens depending upon the nature of the violation (*see* Br. for SEC at 17-20), the Seventy-Third Congress did not differentiate among those provisions when it adopted a uniform one-year/three-year limitations period. It made a universal judgment with respect to the appropriate period of repose and applied it across-the-board. There is *no* evidence that it would have done anything else with a private right under

[11] Although the Commission asserts that the "force" of Congress's rationale in 1934 for adopting the one-year/three-year rule "has significantly diminished" over time (Br. for SEC at 27), it offers nothing to support this assertion other than its own *ipse dixit*. *See* Br. for SEC at 23-28. This Court has in the past resisted the temptation to accord undue weight to such *ex cathedra* pronouncements by the SEC. "Since the language and legislative history of [the 1934 Act] are dispositive" in this case, the Court need not consider the "policy arguments" advanced by the Commission. *Aaron* v. *SEC*, 446 U.S., at 700 n.19; *see also Randall v. Loftsgaarden*, 478 U.S. 647, 656 (1986) (declining to consider policy arguments). Moreover, the Commission's policy arguments, even if they were otherwise sufficiently compelling to convince the Court to repeal the legislative judgments made by the Legislative Branch, do not prove the point for which they are advanced. For example, the Commission (Br. for SEC at 24-25) disagrees with the court's statement in *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1392 (7th Cir. 1990), *cert. pending* (No. 90-526), that "[p]rudent investors almost always can sniff out fraud (or enough smoke to justify litigation) within three years," arguing that "even the SEC . . . does not complete its investigations, on average, in less than 2.25 years." Br. for SEC at 24 n.37. However, the Commission's enforcement actions generally are not governed by *any* statute of limitations (Br. for SEC at 30), and unlike private litigants the Commission enjoys the luxury of conducting a full and complete investigation prior to filing suit. It is therefore meaningless to compare the Commission's average investigatory time-table to the time needed for a private plaintiff to ascertain whether a good faith basis exists for filing a § 10(b) suit.

§ 10(b), and it is against all logic that Congress would have preferred fifty different state laws to define the § 10(b) right over the limitations period it developed for the *"comparable express causes of action."*[12]

C. There are No Suitable State or Federal Alternatives to the One-Year/Three-Year Rule.

1. *Common Law Fraud*

Although respondents claim that "common law fraud is sufficiently analogous to § 10(b) for statute of limitations purposes," their own descriptions of § 10(b) do not support that claim. Respondents concede, as they must, that the "evidentiary" and "procedural" burdens under § 10(b) "were relaxed to enable a plaintiff to more easily prove securities fraud and to extend liability 'to a broader reach than the common law had previously permitted.'" Br. for Resp. at 20-21 n.19 (quoting *Basic Inc.*, 485 U.S., at 253 (White, J., concurring in part and dissenting in part)); *see, e.g., Herman & MacLean*, 459 U.S., at 388 ("[r]eference to common-law practices can be misleading" when interpreting § 10(b)); *see also* Br. for Pet. at 22. Respondents, however, want all the benefits but none of the accouterments of federal law. Indeed, if state common law fraud actions actually were "sufficiently analogous" to § 10(b) actions, there would be little reason for respondents—who also have filed state fraud claims against petitioner—to contend so strenuously in this case for a long statute of limitations for their federal claims.

Respondents also concede that, unlike the express remedies of the 1933 and 1934 Acts, "§ 10(b) arises out of a

[12] *Blue Chip Stamps*, 421 U.S., at 736 (emphasis added). The Commission and respondents argue that the Court "has shaped the private right of action under Section 10(b) with the understanding that the one-and-three year limitations periods do not apply to it." Br. for SEC at 20; Br. for Resp. at 30-31. However, the Court has "shaped" § 10(b) so as to *avoid* "nullify[ing] the effectiveness" of the one-year/three-year statutes of limitations and the express rights of action to which they apply. *Ernst & Ernst*, 459 U.S., at 210 & n.29; *see also Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 384 & n.18 (1983). The same approach in this case would require the endorsement of the one-year/three-year statute of limitations contained in § 9(e) of the 1934 Act for § 10(b) claims.

different historical context than common law fraud." Br. for Resp. at 20-21 n.19. In fact, "the doctrines of fraud and deceit . . . developed around transactions involving land and other tangible items of wealth," *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 194 (1963), an historical context that is "light years away from the world of commercial transactions to which Rule 10b-5 is applicable," *Blue Chip Stamps*, 421 U.S., at 744-45; *see also Basic Inc.*, 485 U.S., at 243-44.

More importantly, selection of state fraud limitations for § 10(b) claims would still leave the courts and the parties to struggle with difficult choice of law questions and would perpetuate "the danger of forum shopping," *Agency Holding Corp.*, 483 U.S., at 154, that currently exists in almost every § 10(b) case. *See* Br. for Pet. at 19-32. Indeed, the statutes of limitations for common law fraud vary dramatically from State to State. For example, the limitations period for fraud is one year in Virginia, *see Pigott* v. *Moran*, 231 Va. 76, 341 S.E.2d 179, 181-82 (1986); two years in Oklahoma, *see Buford White Lumber Co. Profit Sharing & Sav. Plan & Trust* v. *Octagon Properties, Ltd.*, 740 F. Supp. 1553, 1567 (W.D. Okl. 1989); three years in California, *see Davis* v. *Birr, Wilson & Co.*, 839 F.2d 1369, 1369-70 (9th Cir. 1988); four years in Texas, *see Sioux, Ltd., Sec. Litig.* v. *Coopers & Lybrand*, 914 F.2d 61, 63 (5th Cir. 1990); five years in Illinois, *see Martin-Trigona* v. *Champion Fed. Sav. & Loan Ass'n*, 892 F.2d 575, 577 (7th Cir. 1989); and six years in New Jersey, *see Roberts* v. *Magnetic Metals Co.*, 611 F.2d 450, 453 (3d Cir. 1979). In New York, the statute of limitations is two years from discovery of the fraud or six years from the commission of the fraud, whichever is longer, *see IIT* v. *Cornfeld*, 619 F.2d 909, 928-29 (2d Cir. 1980); while in Florida, the limitations periods are four years from discovery of the fraud but no later than twelve years after the fraud was committed, *see Armbrister* v. *Roland Int'l Corp.*, 667 F. Supp. 802, 811 (M.D. Fla. 1987).

In *Wilson* v. *Garcia*, 471 U.S. 261 (1985), upon which respondents rely (Br. for Resp. at 22-24), the Court "bor-

rowed" state personal injury limitations periods for § 1983 civil rights actions. However, the Court's decision in *Wilson* was compelled by 42 U.S.C. § 1988, in which Congress expressly instructed courts engaged in interstitial lawmaking with respect to 42 U.S.C. § 1983 to resort to common law as modified by the statutes and constitution of the forum State. 471 U.S., at 268. *Wilson* was therefore a case in which a federal statute guided the Court to select a state limitations period. *See DelCostello* 462 U.S., at 159 n.13.

Wilson presents a wholly different picture than that raised by § 10(b). Unlike the inevitably interstate nature of § 10(b) litigation, the "typical § 1983 suit" "need not [contain] any nexus to interstate commerce," and such claims "most commonly involve[ ] a dispute wholly within one state." *Agency Holding Corp.*, 483 U.S., at 154; *see Ceres Partners* v. *GEL Associates*, 918 F.2d 349, 360 (2d Cir. 1990); *Short*, 908 F.2d, at 1388; Br. for Resp. at 21 n.19 ("plaintiffs are able to bring class action suits for nationwide securities fraud or maintain actions for securities bought on a national market where such actions would not be possible under traditional common law theories"). The practicalities of § 10(b) litigation, therefore, require a uniform federal rule, and preclude application of a variety of state fraud limitations periods. *Agency Holding Corp.*, 483 U.S., at 153-54.

Section 10(b) presents an even more compelling case for application of a uniform federal statute of limitations than the RICO provision involved in *Agency Holding Corp.*, which created a generic federal civil remedy for "racketeering." Much more so than RICO, the 1933 and 1934 Acts were specifically intended to provide a uniform, federal regulatory scheme for a segment of interstate commerce that is vital to the national economy and to cure the deficiencies of an ineffective, inconsistent and inhibiting system of state-by-state regulation. *See* Br. for Pet. at 11-15. Indeed, "Congress enacted a national rule against fraud because it believed that national law ought to govern multistate transactions. Returning to state law to fetch a

period of limitations is inconsistent with the spirit of this decision." *Short*, 908 F.2d, at 1388.

Respondents also contend that state fraud limitations periods are appropriate for § 10(b) cases because such limitations periods are generally subject to indefinite equitable tolling, while the one-year/three-year period imposes an unacceptable (to respondents) outside limit on when an action may be brought. *See* Br. for Resp. at 19, 31-32.[13] But that is a legislative judgment, peculiarly within the competence of Congress to make and not an appropriate inquiry for interstitial lawmaking. Congress focused considerable attention on the issue and explicitly limited the length of time to a maximum tolling of three years. ABA, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 655 (1986) ("The express limitations periods . . . all contain an absolute cut-off."); Bloomenthal, *supra* note 2, at 21 ("*all* the participants in the debate agreed that the limitation period was . . . *absolute*") (emphasis added).[14]

Respondents' invocation of the "investor-oriented, remedial purpose of the federal securities laws" (Br. for Resp. at 17) is a one-sided perspective on the balancing process and cannot overcome the clear expression of legislative intent. As this Court has often recognized, "generalized references to the 'remedial purposes' of the 1934

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[13] Respondents' objections to the one-year/three-year rule are directed exclusively at the three-year period of repose and its restriction of the equitable tolling doctrine. Indeed, although respondents contend that the one-year/three-year period is "too short" (*see* Br. for Resp. at 17) for application to § 10(b) claims, it is "in fact *not* shorter than most state limitations periods . . . ." *Ceres Partners*, 918 F.2d, at 349 (emphasis added); *see* Br. for Pet. at 25-26.

[14] *See* Br. for Pet. at 37-42. Congress clearly contemplated that the three-year cut-off would apply to "fraud" claims, *see* 78 Cong. Rec. 8198-8201 (May 7, 1934), and, of course, was well aware that fraud could conceivably be hidden for several years, *see, e.g.*, 78 Cong. Rec. 8201 (May 7, 1934) (statement of Sen. Barkley).

Act will not justify reading a provision 'more broadly than its language and the statutory scheme reasonably will permit'." *Touche Ross & Co.*, 442 U.S., at 578 (quoting *SEC* v. *Sloan*, 436 U.S. 103, 116 (1978)); *see also Ernst & Ernst*, 425 U.S., at 200. Respondents urge the Court to focus only on one-half of the equation, the rights of allegedly defrauded investors, but Congress deliberately balanced those interests against the interests of market stability[15] and the interests of repose and reached a legislative judgment that is exclusively the prerogative of Congress to overturn.

2. *The Interstate Land Sales Act*

Aside from the fact that it has an expansive limitations period (Br. for Resp. at 35), there is nothing to commend the 1979 amendments to the Interstate Land Sales Act ("ILSA"), 15 U.S.C. § 1701, *et seq.*, as a source for a limitations period in securities fraud cases.

Because the 1934 Act itself supplies clear guidance regarding the appropriate limitations period for § 10(b) claims, "there is no room for the argument" that other statutes should be consulted for interpretive guidance. *Greenport Basin & Construction Co.* v. *United States*, 260 U.S. 512, 516 (1923); *see also Erlenbaugh* v. *United States*, 409 U.S. 239, 244-45 (1972). Futhermore, the ILSA, which deals with fraud in connection with interstate land sales, does not "pertain to the same subject" as § 10(b), *Erlenbaugh*, 409 U.S., at 243, and therefore cannot serve as a guide to § 10(b)'s interpretation. *See Fort Stewart Schools* v. *Federal Labor Relations Authority*, 110 S. Ct. 2043, 2047 (1990).

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[15] A principal objective of the federal securities laws was to protect and stablize the national securities markets and the national economy. *See Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 315 (1985); *United States* v. *Naftalin*, 441 U.S. 768, 775 (1979). State fraud limitations periods, of course, were not devised with these "national interests in mind." *Occidential Life Insurance Co.* v. *EEOC*, 432 U.S. 355, 367 (1977).

Respondents cite *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S., at 386, in support of the proposition that "[c]ongressional intent embodied in a statute with similar purposes is relevant." Br. for Resp. at 34 n.40. In that case, however, the Court concluded that the Investment Advisers Act of 1940 was to be construed consistently with "other securities legislation," *id.*, at 195, including the 1933 and 1934 Acts. But that logic supports consulting the 1933 and 1934 securities acts, not a 1979 land sales statute. In fact, the Court in *Capital Gains* expressly recognized that "doctrines of fraud and deceit which developed around transactions involving *land . . . are ill-suited* to the sale of . . . securities." *Id.*, at 194 (emphasis added). Thus, *Capital Gains* supports application of the one-year/three-year rule, not the ILSA limitations period, to § 10(b) claims.

3. *Section 20A of the ITSFEA*

The Commission's contention that § 20A of the Insider Trading and Securities Fraud Enforcement Act of 1988 ("ITSFEA"), 15 U.S.C. § 78t-1, is "more analogous" to § 10(b) than any of the express rights of action governed by the one-year/three-year rule (Br. for SEC at 17) is completely without merit. It has been rejected by every court to consider it. *See* Br. for Pet. at 47-48. Even respondents concede that § 20A is not broad enough to be analogous to § 10(b) and that "Congress made it as clear as possible" that § 20A's limitations period "should not apply to § 10(b) claims beyond the scope of § 20A." Br. for Resp. at 42.

This Court has already determined that § 10(b) can and should be interpreted in conjunction with the "comparable express causes of action"[16] contained in the 1933 and 1934 Acts. They are interrelated components of a comprehensive statutory scheme designed to combat fraudulent and manipulative practices in the national securities markets. *See Herman & MacLean*, 459 U.S., at 383-86. "All aim to

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[16] *Blue Chip Stamps*, 421 U.S. at 736.

compensate the same type of injury. All are designed to fill a void in the common law and to create remedies that would be uniform throughout our nation's commerical universe . . . ." *In re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1548-49 (3d Cir.) (*en banc*), *cert. denied*, 488 U.S. 849 (1988). The Commission's policy arguments for a longer limitations period, which should, in any event, be addressed to Congress, fail to take into account the cohesive and complementary structure of the antifraud provisions of the securities laws enacted by the Seventy-Third Congress, and the unity of purpose that animates them.

As the Commission acknowledges (*see* Br. for SEC at 13-14 & n.15), § 20A was appended to this scheme 54 years later *solely* to respond to a specific, narrow category of cases arising under the securities laws—insider trading cases involving "misappropriation" of material nonpublic information. While § 20A applies only to a limited class of defendants who trade "contemporaneously" with plaintiffs in the same "class of securities" based upon material, nonpublic information,[17] § 10(b) claims "can be brought by a purchaser or seller of '*any* security' against '*any* person' who has used '*any* manipulative or deceptive device or contrivance,' " *Herman & MacLean*, 459 U.S., at 382 (emphasis in original). Section 10(b) thus embraces a broad array of fraudulent practices (Br. for SEC at 23) that have "no relationship" to insider trading. *Ceres Partners*, 918 F.2d, at 363.

Section 20A authorizes an action for conduct prohibited by § 10(b), but also for violations of other provisions of the securities laws, including § 14(e) of the 1934 Act, 15 U.S.C. § 78n(e). *See* 15 U.S.C. § 78t-1(a) (creating private action against "[a]ny person who violates any provision of this title"); H.R. Rep. No. 910, 100th Cong., 2d Sess., *reprinted in* 1988 U.S. Code Cong. & Admin. News 6043, 6045 ("insider trading" is prohibited by "Section 17(a) of

[17] 15 U.S.C. § 78t-1(a). According to the Commission, § 20A was not even intended to encompass all of the insider trading actions that can be brought under § 10(b). Br. for SEC at 26-27.

the Securities Act, Sections 10(b) and 14(e) of the Securities Exchange Act of 1934 and Section 206 of the Investment Advisers Act"). Accordingly, § 20A does not, as the Commission contends (Br. for SEC at 13), "require the plaintiff to establish the same elements" as § 10(b).[18]

Thus, § 20A is at once narrower and broader than § 10(b). There is simply no logic to the contention that this peculiar, hybrid remedy should be an indirect vehicle for the creation of a five-year limitations period for § 10(b) actions.

The Commission's argument that adoption of a one-year/three-year limitations period would "engender confusion" by giving plaintiffs "an incentive to engage in 'artful pleading' " (Br. for SEC at 25-26) to obtain the advantages of § 20A's longer limitations period, was cogently answered by the Seventh Circuit in *Short*:

> To obtain the five-year period of § 20A, the plaintiff would have to sue under § 20A, establish trading by an insider . . . , and accept the limitations of that statute, including the restriction of damages to the defendants' profit (as opposed to the plaintiff's loss).

908 F.2d, at 1391. Moreover, there is a far greater risk that if § 10(b) claims are subject to a five-year limitations period, plaintiffs inevitably will plead alleged violations of the express remedies as § 10(b) claims in order to avoid the one-year/three-year limitations periods. *See* Br. for Pet. at 48.

The Commission's argument that the Court should rely upon Congress's "accommodation of policies" in 1988 (Br.

[18] *Compare Dirks* v. *SEC*, 463 U.S. 662 (1983) (§ 10(b) plaintiffs must demonstrate scienter and breach of a fiduciary duty to establish insider trading claim) *with United States* v. *Chestman*, 903 F.2d 75, 84-85 (2d Cir. 1990) (Mahoney, J., concurring in part and dissenting in part) (expressing the view that under SEC Rule 14e-3 scienter is not required and "there is no requirement that any fiduciary duty exist or be violated"), *reh'g en banc granted*, Aug. 25, 1990.

for SEC at 15, 23-24), rather than the accommodation of policies of the Seventy-Third Congress when it enacted § 10(b), ignores fundamental principles of statutory construction. It is the intent of the Congress that enacted the 1934 Act that properly governs the interpretation of a provision of that Act. *See Touche Ross & Co.* v. *Redington*, 442 U.S., at 574-75 n.16 ("[g]iven the fact that our task is to discern the intent of Congress when it enacted § 17(a) in 1934, we doubt the relevance of [subsequent legislation] to our inquiry"); *SEC* v. *Capital Gains Research Bureau, Inc.*, 375 U.S., at 199-200 (determining that the "intent of Congress must be culled from the events surrounding the [Investment Advisers Act of 1940]," rather than amendments to that legislation in 1960. " '[O]pinions attributed to a Congress twenty years after the event cannot be considered evidence of the intent of the Congress of 1940.' ") (citation omitted).[19]

D. Petitioner is Entitled to the Benefits of the One-Year/Three-Year Rule in this Case.

Respondents argue that any limitations period adopted in this case "should only be applied prospectively." Br. for Resp. at 46. However, given the Court's well-settled "policy of applying the rule it announces to the parties before the Court," *Goodman* v. *Lukens Steel Co.*, 482 U.S. 656, 689-90 (1987) (O'Connor, J., concurring in part and dissenting in part), the Court need not examine the issue of retroactivity in this case.[20] *See, e.g., DelCostello*, 462

[19] Despite its disclaimers regarding the interpretive value of the intent of the Seventy-Third Congress, the Commission switches direction and relies upon the legislative history of the 1934 Act and the language of the express limitations periods enacted in 1934 to support its argument that § 20A's five-year limitations period is not subject to equitable tolling. Br. for SEC at 28-29.

[20] *See Stovall* v. *Denno*, 388 U.S. 293, 301 (1966) ("Sound policies of decision-making, rooted in the command of Article III of the Constitution that we resolve issues solely in concrete cases or controversies, and in the possible effect upon the incentive of counsel to advance contentions requiring a change in the law, militate against denying [petitioners] the benefit of today's decisions."); *see also American Trucking Associations, Inc.* v. *Smith*,

U.S., at 172 (applying new, shorter federal limitations period to bar the claims of respondents).

Moreover, even if a retroactivity analysis were appropriate in this case, respondents' arguments under the three-prong inquiry of *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971), are without merit. The threshold inquiry under *Chevron* is whether "the decision . . . establish[ed] a new principle of law . . . by overruling clear past precedent *on which litigants may have relied.*" *Id.*, at 106 (emphasis added). Generally, unless the first *Chevron* factor is satisfied, " 'there is no occasion to consider the other two'." *Welch* v. *Cadre Capital*, No. 10-7419 (2d Cir. Jan. 22, 1991), slip op., at 1441 (citation omitted).

Respondents do not and cannot claim that they detrimentally relied upon past precedent in this case. They purchased their limited partnership interests during the period October 1979 and June 1981, and allege that they did not discover their § 10(b) claims until March 1986. J.A. 40, 89, 106, 122, 146, 161, 177, 192, 208, 224, 250. Thus, respondents, by their own admission, did not delay the filing of their claims in reliance upon past precedent because the three-year period of repose had already expired when they purportedly discovered petitioner's alleged violation of § 10(b).[21] *See, e.g., Gatto* v. *Meridian Medical Associates, Inc.*, 882 F.2d 840, 843 (3d Cir. 1989) ("[b]ecause appellants did not know the significant oper-

110 S. Ct. 2323, 2345 (1990) (Scalia, J., concurring in the judgment) ("the limitation of the Case or Controversy requirement of Article III . . . surely requires retroactivity with respect to the parties immediately before the Court"); *Rodriguez de Quijas* v. *Shearson/American Express*, 490 U.S. 656, 662 (1989) ("The general rule of long standing is that the law announced in the Court's decision controls the case at bar.").

[21] Although respondents now speculate that they might have been more diligent in investigating the facts surrounding the transactions at issue had they known that their claims were subject to a three-year statute of repose (Br. for Resp. at 48 n.65), their claims under the Oregon securities laws *were* subject to a three-year repose period, *see Ore. Rev. Stat.* 59.115 (1979) (amended in 1985 to permit tolling), but respondents nonetheless delayed filing those claims until November 1986.

ative facts underlying their cause of action . . . until after the three year absolute bar period of *Data Access* had passed, they could not possibly have relied on a longer statute of limitations period"), *cert. denied*, 110 S. Ct. 1136 (1990); *see also Short*, 908 F.2d, at 1390 ("[plaintiff] cannot have relied on Illinois law because she claims to have been unaware of the basis for litigation until a short time before filing suit").[22] Consequently, respondents cannot establish the first *Chevron* criteria—detrimental reliance—and their argument against retroactive application of the one-year/three-year limitations period must fail.[23]

E. Conclusion

As a leading commentator has observed with respect to the § 10(b) implied right of action,

> with the 1933 and 1934 Acts so closely related, why not look to *their* statutes of limitations by way of analogy rather than to a variant state law? Would it not be eminently more consistent with the overall statutory scheme to look to what Congress itself did when it was thinking specifically of private actions in securities cases rather than to a grab-bag of . . . state statutes?

L. Loss, *supra* note 6, at 995 (emphasis in original). The Court should answer that question in the affirmative and select the one-year/three-year limitations period of § 9 of the 1934 Act for § 10(b) claims.

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[22] *Cf. Welch* v. *Cadre Capital*, *supra*, slip op. at 1434-35 (declining to apply *Ceres Partners* retroactively where plaintiffs discovered claims *before* three-year period had expired, but delayed filing suit in conformance with state law).

[23] Respondents' arguments with respect to the other *Chevron* factors also are without merit. Since respondents did not rely upon the practice of applying state limitations periods, application of the one-year/three-year limitations period will not "produce substantial inequitable results," *Chevron*, 404 U.S., at 106, but rather will produce precisely the results intended by the Seventy-Third Congress by precluding litigation of securities fraud claims more than three years after the alleged violation occurred. *See Goodman*, 482 U.S., at 663-64; *Gatto*, 882 F.2d, at 844.

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No. 90-333

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,

Petitioner,

-v.-

JOHN GILBERTSON *ET AL.*,

Respondents.

On Writ of Certiorari
to the United States Court of Appeals
for the Ninth Circuit

BRIEF FOR AMERICAN COUNCIL OF LIFE INSURANCE AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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BRIEF FOR AMERICAN COUNCIL OF LIFE INSURANCE AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

INTEREST OF THE *AMICUS*

The American Council of Life Insurance (hereinafter "Council") is the largest non-profit life insurance trade association in the United States. Its membership of 635 life insurance companies holds, in the aggregate, 95% of the assets of all the United States life insurance companies. Life insurance companies are among the

country's major financial intermediaries and are, therefore, engaged continually in the purchase and sale of securities. For that reason, they are likely to be involved, either as plaintiffs or defendants, in actions brought under Section 10 of the Securities Exchange Act of 1934 and Rule 10b-5. They have an interest, accordingly, in the elimination of the uncertainty and confusion that now exists with respect to the limitations periods applicable to such actions and in the establishment of a uniform and appropriate limitations period. This case offers the Court the opportunity to achieve that objective.[1/]

SUMMARY OF ARGUMENT

The ACLI strongly supports petitioner's principal arguments in this case: (1) that the appropriate limitations period for actions under Section 10 of the Securities Exchange Act of 1934 (the 1934 Act) should be found in federal rather than state law and (2) that the appropriate federal limitations period for such actions is the one-year/three-year provision found in Section 9(e) of the 1934 Act. Since we have little to add to the petitioner's brief and the briefs of the other *amici* on these issues, Parts I and II limit themselves to very brief comments about certain aspects of those two issues. We suggest, in Part I, that rather than creating a few exceptions to the general rule that limitations periods for federal actions will be found, when needed, in analogous state statutes, this Court has been moving toward establishing a sounder, more rational rule, and should

1/ The written consents of the parties to the filing of this brief have been filed with the Clerk of the Court.

continue to do so. In Part II we contend that the reasons offered by the Securities and Exchange Commission for adopting a five-year limitations period are unpersuasive.

In Part III, we argue that it is wholly appropriate for the Court to provide guidance to the lower courts that must apply the factors in *Chevron Oil Co.* v. *Huson*, 404 U.S. 97, 106-07 (1971), in determining whether the ruling that we anticipate in favor of the federal limitations period found in Section 9(e) of the 1934 Act should be applied retroactively or prospectively only. In particular, we urge the Court to make clear that no Circuit authority in favor of a different state limitations period could be considered "established" once the bar was on notice of this Court's decision in *Agency Holding Corp.* v. *Malley-Duff & Associates*, 483 U.S. 143 (1987). Such guidance would provide a uniform and desirable base point for retroactivity analysis and greatly minimize unnecessary litigation.

ARGUMENT

I. The Appropriate Limitations Period for Section 10 Actions Should Be Found in Federal Rather Than State Law.

This case provides the Court with another opportunity, following *DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151 (1983), *Agency Holding Corp.* v. *Malley-Duff & Associates*, 483 U.S. 143 (1987), and *Reed* v. *United Transportation Union*, 488 U.S. 319 (1989), to continue the process of reducing the confusion and

uncertainty concerning the periods of limitations applicable to claims for relief established by federal law. Justice Scalia, in an erudite concurrence in *Agency Holding*, a civil RICO action, showed how the rationale for the "general rule" -- that where Congress has inexplicably failed to provide a limitations period for a civil action expressly created by statute (and, necessarily, where there is no limitations period for an implied right of action), the period applied by the forum state to the most similar state action will be applied -- has changed dramatically since this rule was first adopted. Justice Scalia, however, argued against further change, and against the adoption of a sounder rationale, one that would eliminate the inconsistent and unpredictable results that application of this general rule has spawned.[2/]

The modest change in the general rule effected by *DelCostello*, *Agency Holding*, *Wilson* v. *Garcia*, 471 U.S. 261 (1985), and *Reed* v. *United Transportation Union*, is based, we submit, upon a fundamental change in the rationale for the rule. Where it appears, as it does in many cases, that Congress has simply failed, inexplicably, to adopt a limitations period, the Court no longer presumes that Congress intended that courts borrow the analogous state limitations period. Rather, the Court recognizes, correctly in our view, that with an aberrant exception or two, a limitations period for a civil action is an integral part of the "genius of our laws," *Adams* v. *Woods*, 6 U.S. (2 Cranch) 336, 342 (1805), and that the

2/ The opinion of the Court of Appeals for the Second Circuit in *Ceres Partners* v. *GEL Associates*, __ F.2d __ (No. 89-7666) (Nov. 8, 1990), describes in detail the confusion that the general rule has caused in that circuit, in actions brought under Section 10 of the 1934 Act and Rule 10b-5.

adoption of an appropriate period is as much a part of the "interstitial lawmaking" of the federal common law (*DelCostello*, 462 U.S. at 172) as the fashioning of the substantive elements of the federal claims for relief established expressly or impliedly by Congress.[3/]

We see no reason to paraphrase or summarize here the extensive demonstrations that will be made in the briefs of the petitioner and of other *amici*, and which have already been made in the well considered opinions of three courts of appeals that have considered this issue, that explain why federal law, more particularly the Securities Exchange Act of 1934, "'clearly provides a closer analogy than available state statutes.'" *Reed* v. *United Transportation Union*, 488 U.S. at 324 (quoting *DelCostello*, 482 U.S. at 172).

II. The Limitation Period Provided for Actions Brought Under Section 9 of the Exchange Act Should Be Adopted for Actions Brought Under Section 10.

Similarly, we believe we can add little to the briefs that will be filed by the petitioner and supporting *amici* on the issue of whether actions authorized by Section 9(e) of the 1934 Act provide the closest analogy to actions under Section 10 of that Act, so as to make appropriate the adoption of the one and three year limitations periods set forth in Section 9. We limit ourselves, therefore, to a brief comment upon the position urged in

3/ The requirement of scienter on the part of the defendant, first set forth in *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976), is an apposite example of the development of a federal common law that gives content to a broad and generally phrased statute.

the *amicus* brief that we are advised will be filed by the Securities and Exchange Commission. The Commission contends that this Court should apply here the five-year limitations period set forth in Section 20A of the 1934 Act, added by the Insider Trading and Securities Fraud Enforcement Act of 1988. Prior to the 1988 Act, claims based upon the improper use of non-public material information had indeed been brought under Rule 10b-5, and the 1988 Act was intended both to codify the court decisions upholding such actions and to overturn others which had denied relief in certain circumstances. H.R. Rep. No. 910, 100th Cong., 1st Sess. 26 (1988). That Act also provided for the same five-year limitations period already applicable to treble damage actions brought by the Commission under the Insider Trading Sanctions Act of 1984. See H.R. Rep. No. 355, 98th Cong., 2nd Sess. 30 (1984).

The Commission's position (based upon our reading of earlier *amicus* briefs filed by it) appears to rest largely upon its belief that private rights of action are an important part of the enforcement of the securities laws and that the longer the limitations period the better the enforcement. This approach ignores altogether the doctrine laid down by this Court in the cases cited above. It is rather the most closely analogous limitations period that must be sought and not the one that favors plaintiffs who have delayed filing their actions and that problematically supports the policies of the Act.[4/]

4/ In many cases it would be possible for a plaintiff with a possibly sound claim under Rule 10b-5 to wait to see whether the price of a security increases to the point where the profits exceed the probable damage. Providing plaintiffs with such a "free ride" is assuredly not one of the policies of the 1934 Act.

There is no basis, moreover, for the conclusion that the longer the limitations period the better served investors and the public will be. Long ago this Court emphasized that statutes of limitation are entitled to strict enforcement and that protection against stale claims and the consequent unavailability of relevant evidence effectuates a significant public policy.

> "Statutes of limitation are vital to the welfare of society and are favored in the law. They are found and approved in all systems of enlightened jurisprudence. They promote repose by giving security and stability to human affairs. An important public policy lies at their foundation. They stimulate to activity and punish negligence. While time is constantly destroying the evidence of rights, they supply its place by a presumption which renders proof unnecessary. Mere delay, extending to the limit prescribed, is itself a conclusive bar. The bane and antidote go together." *Wood* v. *Carpenter*, 101 U.S. 135, 139 (1879).

Finally, it should be noted that when the Insider Trading and Securities Fraud Enforcement Act was under consideration, the Commission was surely aware of this Court's decisions in *DelCostello* and *Agency Holding*. It was also aware of the extensive criticism of the "borrow from the states" doctrine in Rule 10b-5 cases set forth in the American Bar Association's *Report of the Task Force on Statute of Limitation for Implied Actions*, 41 Bus. Law. 645 (1986) and, indeed, it appears that the Commission shared the views of the ABA. The Commission was aware that the bill under consideration provided a limitations period for contemporaneous insider trading actions.

It was aware, finally, of the remarkably close similarity of the express right of action under Section 9, in respect of transactions in exchange-listed securities, to the implied right of action under Section 10 in respect of transactions in other securities. Had the Commission believed a five-year limitations period to be appropriate, it would have been simple enough to suggest to the Congress that it consider the adoption of a limitations period for all Section 10 actions. In the absence of any such suggestion or independent action by the Congress, however, it must be assumed that the Commission and the Congress expected the doctrines set forth in the recent decisions of this Court to be applied. That expectation should now be fulfilled.

III. The Court Should Eliminate Continued Uncertainty and Confusion by Providing Guidance as to the Retroactive Applicability of Its Decision.

Assuming that this Court accepts petitioner's argument and adopts the one-year/three-year statute of limitations in § 9(e) of the Securities Exchange Act for Rule 10b-5 actions, respondents have represented that they will ask the Court to rule that the decision should not be applied retroactively to their own circumstances. Br. in Opp. at 10. We leave that issue to the briefs of the parties. We urge the Court, however, to make clear that its holding is, at the very least, retroactive to the date of decision in *Agency Holding Corp.* v. *Malley-Duff & Associates*, 483 U.S. 143 (1987) -- June 22, 1987.

We recognize that, under other circumstances, the question of whether a new rule that overturns another of

long standing should be applied prospectively or retroactively is left to the lower courts, to be determined by the application of the factors set forth in *Chevron Oil Co.* v. *Huson*, 404 U.S. 97, 106-07 (1971). That is because, as the Court will recall, the issue may be determined differently in different jurisdictions depending upon the state of the applicable law at the time the actions were brought. Here, as we shall show, application of *Chevron* calls for a uniform nation-wide rule, so it is particularly appropriate for the Court to discuss this matter in its opinion. Otherwise, there will be continued litigation over retroactivity and, in many cases, over which state law to apply. Since one result of a decision by this Court to apply the limitations provision of Section 9(e) -- and perhaps also an objective of the decision -- will be to eliminate the unfortunate morass that the past 40 years have created, it would further the desirable effect of the decision by bringing the unnecessary litigation to an end sooner, rather than later.

Chevron Oil set forth three factors for deciding whether a court decision should be applied retroactively or prospectively only: (1) whether the decision establishes "a new principle of law, either by overruling clear past precedent on which litigants may have relied * * * or by deciding an issue of first impression whose resolution was not clearly foreshadowed"; (2) whether retroactive operation of the rule in dispute "'will further or retard its operation'"; and (3) whether retroactive operation of the rule "'could produce substantial inequitable results.'" 404 U.S. at 106-07 (citations omitted). See *Northern Pipeline Construction Co.* v. *Marathon Pipe Line Co.*, 458 U.S. 50, 87-88 (1982). The Court in *Chevron* applied those factors to hold that a one-year state statute of limitations

made applicable to plaintiff's off-shore injury by the then-recent decision of this Court in *Rodrigue* v. *Aetna Casualty & Surety Co.*, 395 U.S. 352 (1969), should not be made applicable to a pre-*Rodrigue* case, where *Rodrigue* had effectively overruled a long line of decisions by the Fifth Circuit. The Court explained the rationale for its decision: "It cannot be assumed that [plaintiff] did or could foresee that this consistent interpretation of the Lands Act would be overturned." 404 U.S. at 107.

More recently, in 1987, this Court reviewed two decisions of the Third Circuit relating to the retroactivity of that Circuit's ruling, in light of *Wilson* v. *Garcia*, 471 U.S. 261 (1985), that § 1981 actions in Pennsylvania are governed by that State's two-year limitations period governing personal injury actions, rather than that state's six-year statute of limitations. In *Saint Francis College* v. *Al-Khazraji*, 481 U.S. 604 (1987), this Court affirmed the Third Circuit's decision that plaintiffs' action, brought in 1980, was not time-barred under the new rule, finding the Third Circuit's decision an appropriate application of the *Chevron Oil* rule that a newly applicable statute of limitations should be applied only prospectively when the Court "overruled clearly established Circuit precedent on which the complaining party was entitled to rely * * *." 481 U.S. at 608. In the second case, *Goodman* v. *Lukens Steel Co.*, 482 U.S. 656 (1987), this Court affirmed a contrary decision by the Third Circuit to apply the new rule to plaintiffs' case, which had been filed in 1973, at which time "'there was no established precedent in the Third Circuit to indicate the appropriate limitations period for Section 1981 claims.'" 482 U.S. at 663, quoting the Third Circuit decision.

In a very recent decision, *American Trucking Associations, Inc.* v. *Smith*, 110 S. Ct. 2323 (1990), this Court reaffirmed the *Chevron* approach. "As *Chevron Oil* makes clear, the purpose of the doctrine is to avoid '"injustice or hardship"' to civil litigants who have justifiably relied on prior law." 110 S. Ct. at 2342.

These decisions make clear that, if this Court should decide that the one-year/three-year provision in § 9(e) of the 1934 Act governs Rule 10b-5 actions, the decision should be applied retroactively to suits brought prior to the date of the decision, except in those instances when potential plaintiffs might reasonably have relied on established Circuit precedent that specified a different statute of limitations. As we suggest above, what constituted "established Circuit precedent" should, at least after June 1987, be decided in the same way in every Circuit rather than on a Circuit by Circuit basis.

The Court's decision in *Agency Holding* was a clear signal to the bar, and particularly to the securities bar, that the appropriateness of borrowing a state statute of limitations for Rule 10b-5 actions -- an issue that had not yet been decided by this Court -- was an open question. In that case, the Court found significant that a 1985 American Bar Association RICO task force had "described the current state of the law regarding the applicable statue of limitations for civil RICO claims as 'confused, inconsistent, and unpredictable,'" 483 U.S. at 148, and concluded that "a uniform statute of limitations is required to avoid intolerable 'uncertainty and time-consuming litigation.'" *Id.* at 150, quoting *Wilson* v. *Garcia*, 471 U.S. at 272. Because RICO cases commonly involve interstate transactions, and thus the statute of

limitations of several States could govern any given RICO claim, and because there was "no comparable single state law analogue to RICO," 483 U.S. at 152, the Court in *Agency Holding* concluded that the "federal policies at stake and the practicalities of litigation" counseled in favor of the limitations period of the analogous Clayton Act as "a significantly more appropriate statute of limitations than any state limitations period." *Id.* at 153.

The implications of this analysis for Rule 10b-5 actions must have been apparent to every competent lawyer as soon as the decision became widely known. Another ABA task force had just published (in February 1986) a report on the statutes of limitations for Rule 10b-5 actions, demonstrating that application of state statutes of limitations in such actions has "resulted in myriad inconsistent federal court decisions," in "disarray" that "serves no public purpose," and in "uncertainty and lack of uniformity" that promotes forum shopping by plaintiffs and results in "wholly unjustified disparities in the rights of parties litigating identical claims in different states." Committee on Federal Regulation of Securities, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 646-47 (1986). Indeed, the report went on, "Vast amounts of judicial time and attorneys' fees are wasted," and "managements of publicly held companies, as well as their auditors and attorneys, are frequently unable to assess the impact of possible litigation under rule 10b-5." *Id.* at 647.

The extent to which this accurate description of the relevant history points directly to the adoption of a federal limitations period in this case is of course explained at length in the briefs of the parties, and we

shall not elaborate further. The point is simply that after the announcement of the decision in *Agency Holding*, on the heels of this well-publicized ABA report, any competent lawyer, contemplating the filing of a Rule 10b-5 action and looking at the applicable limitations period, would necessarily have concluded that current reliability of existing Circuit authority -- no matter how apparently well-established -- was now in doubt, and would remain in doubt until this Court decided a case such as this one or possibly until a number of circuits had revisited the matter, made uniform decisions, and this Court, by repeated denials of certiorari, signalled that it was not likely to act further.

In the typical case, a potential Rule 10b-5 plaintiff will consult a lawyer about the possibility of suing. Under Rule 11 of the Federal Rules of Civil Procedure, the lawyer or party signing a pleading is responsible for ensuring that there has been "reasonable inquiry" to establish, *inter alia*, that the lawsuit is well-grounded in fact. Since the amount of time available for such inquiry depends on the applicable statute of limitations, any lawyer will attempt to determine as soon as possible what statute of limitations applies. Such a lawyer, after *Agency Holding*, would have recognized that existing Circuit authority was now in doubt.[5/] This conclusion is

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5/ In fairness to lawyers and their clients, we do not believe that established Circuit court authority adopting a state statute of limitations for Rule 10b-5 actions became unsettled on the very date of the decision in *Agency Holding*, June 22, 1987. Because the decision was not, in fact, in the securities area, a decent interval should be allowed during which reliance on established Circuit court authority remains presumptively reasonable. We suggest three months after the *Agency Holding* decision for the length of such "grace period."

confirmed by the speed with which the Third Circuit was urged to read *Agency Holding* as requiring adoption of the federal one-year/three-year limitations period for Rule 10b-5 actions and the speed with which that Court -- less than one year after *Agency Holding* -- agreed. *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir., April 8, 1988) (*en banc*), *cert. denied sub. nom. Vitiello v. I. Kahlowsky & Co.*, 488 U.S. 849 (1988).[6]

Accordingly, this Court should make clear in its decision in favor of the one-year/three-year statute of limitations in § 9(e) of the 1934 Act that its ruling will be retroactive, at the very least, to the date of general publication of this Court's decision in *Agency Holding*.

CONCLUSION

For the foregoing reasons, the American Council of Life Insurance respectfully submits that this Court should rule that the one-year/three-year statute of limitations in Section 9(e) of the Securities Exchange Act of 1934 is applicable to Rule 10b-5 actions and further that it should provide the guidance suggested above to the lower

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6/ The rule that we urge the Court to adopt is consistent with the holdings in *Saint Francis College*, *supra*, because the action in that case had been brought in 1980, well before this Court's 1985 decision in *Wilson* v. *Garcia* put lawyers on notice that civil rights actions under statutes closely related to § 1983 were likely to be subjected to the state statutes of limitation applicable to personal injury claims, in spite of existing circuit court authority to the contrary. Thus this Court did not rule that lawyers can continue to rely on circuit authority even when a recent decision of the Supreme Court has put that authority in serious question.

courts with respect to the retroactive applicability of its decision.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW, PETITIONER

v.

JOHN GILBERTSON, ET AL., RESPONDENTS

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF OF ARTHUR ANDERSEN & CO., COOPERS & LYBRAND, DELOITTE & TOUCHE, ERNST & YOUNG, KPMG PEAT MARWICK, AND PRICE WATERHOUSE AS AMICI CURIAE IN SUPPORT OF PETITIONER

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QUESTION PRESENTED

Whether implied private civil actions under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5 promulgated thereunder (17 C.F.R. § 240.10b-5), should be governed by the statute of limitations prescribed by the 73rd Congress for express causes of action created contemporaneously with the enactment of Section 10(b).

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In the Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-333

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW, PETITIONER

v.

JOHN GILBERTSON, ET AL., RESPONDENTS

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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BRIEF OF ARTHUR ANDERSEN & CO., COOPERS & LYBRAND, DELOITTE & TOUCHE, ERNST & YOUNG, KPMG PEAT MARWICK, AND PRICE WATERHOUSE AS AMICI CURIAE IN SUPPORT OF PETITIONER

INTEREST OF THE AMICI CURIAE

The amici curiae are professional firms engaged in the practice of accountancy. They are the six largest firms of independent accountants in the United States, reporting, collectively, on the financial statements of more than 90 percent of those companies whose securities are publicly traded in the United States. The amici, which are organized as partnerships, are collectively composed of nearly 9,000 partners and more than 78,000 other professional employees, and practice in some 600 offices throughout the United States.

The Securities Act of 1933 and the Securities Exchange Act of 1934 require all public companies whose securities are registered with the Securities and Exchange Commission to have their financial statements examined by independent accountants. See 15 U.S.C. § 77aa (Schedule A) (25)-(27); *id.* § 78*l*(b)(1)(J)-(K). When a registrant or its officers and directors are sued under the federal

securities laws, including Section 10(b), 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5, on the claim that statements issued by the registrant were fraudulent, the registrant's independent accountants frequently are joined as defendants on the basis of allegations that financial statements they audited contained material misstatements or omissions. Because amici's operations are nationwide in scope and amici are subject to suit throughout the country, the current disarray regarding the statute of limitations applicable to actions under Section 10(b) imposes a particularly heavy burden on amici. Amici therefore have a special interest in a uniform and appropriate statute of limitations for actions under Section 10(b) and believe that their views may be of assistance to the Court's consideration of this case.

SUMMARY OF ARGUMENT

The disagreement among the courts of appeals regarding the statute of limitations applicable to Section 10(b) claims creates tremendous uncertainty, leads to disparities in the rights of parties litigating the identical federal claim in different states, promotes forum shopping by plaintiffs, and wastes the resources of litigants and of the courts. "Both the bar and scholars * * * have pleaded, with a unanimity rare in the law, for help." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987). The present state of affairs is a consequence of the failure to apply to Section 10(b) claims the express limitations rule that Congress prescribed for private actions under the securities laws like the action implied under Section 10(b). This Court should hold that Section 10(b) claims are subject to that statute of limitations, which Congress adopted along with Section 10(b) in the Securities Exchange Act of 1934: suit must be brought within one year after discovery of the facts constituting the violation but no later than three years after the transaction in question.

A. Where Congress intended that a particular limitations rule apply to a federal cause of action, that, of course, is the rule that should govern. Here, there can be no doubt that the 73rd Congress—the Congress that enacted Section 10(b)—would have intended to subject any private action implied under Section 10(b) to the one year/three year rule. That is the statute of limitations that applies to every express private action requiring proof of culpability that the 73rd Congress created in the 1934 Act and in the Securities Act of 1933. And the claims that may be brought under those express actions are closely related to the claims that historically have been brought under Section 10(b). Indeed, the very same claim frequently is brought under both Section 10(b) and one or more of these express causes of action. Congress plainly would have subjected all of these claims to the same limitations rule if it had anticipated that the courts would imply a private right of action under Section 10(b).

Moreover, the legislative history reveals that Congress in 1934 carefully considered the appropriate limitations rule. Its adoption of the one year/three year rule was not tied to the specific contours of the express causes of action, but rather reflects a generic determination regarding the appropriate statute of limitations for private actions grounded in claims of securities fraud. That judgment obviously encompasses the action subsequently implied under Section 10(b).

B. Even if the Court chooses to analyze the question by determining which limitations rule supplies the "close[st] analogy" to Section 10(b) (*DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151, 172 (1983)), the one year/three year rule is the obvious choice. First, it is clear that the statute of limitations rule applicable to a claim under Section 10(b) should not vary depending on the particular facts of the claim. The cause of action encompasses a variety of claims that skillful lawyers can characterize in different ways. In order to avoid uncertainty and wasteful litigation, all Section 10(b) claims should be treated the same for statute of limitations purposes.

Second, that statute of limitations should be drawn from federal rather than state law. No state law analogy comes close to capturing all facets of the Section 10(b) action, while the express causes of action under the federal securities laws supply extremely apt analogies. Moreover, the interstate nature of the transactions covered by Section 10(b) and the goals of preventing forum shopping and treating similarly situated parties alike weigh strongly in favor of a uniform federal rule. Plaintiffs now may obtain the benefit of a favorable statute of limitations by choosing a particular forum. And, "if two suits are brought in different states seeking damages for a single act in violation of the federal securities laws, one suit may be barred while the other is not." *Ceres Partners* v. *GEL Associates*, No. 89-7666, slip op. 7253 (2d Cir. Nov. 8, 1990).

Third, the federal limitations rule should be the one year/three year rule adopted by Congress for express causes of action enacted at the same time as Section 10(b), not (as the Securities and Exchange Commission has recently argued) the five year statute that Congress adopted 54 years later to apply only to the narrow category of insider trading claims. See Section 20A(b)(4) of the 1934 Act, 15 U.S.C. § 78t-1(b)(4). Section 10(b) is much more analogous to the actions covered by the one year/three year rule than to the specific and narrowly-drawn remedy set forth in Section 20A. And the legislative history of Section 20A makes clear that the five year statute was designed specifically for the insider trading context; indeed, Congress did not alter the limitations rule for the other express remedies. The one year/three year rule, by contrast, was selected by Congress as a general statute of limitations for securities fraud claims. Because it is "the statute *designed for* the kind of conduct about which * * * most * * * 10b-5 plaintiffs complain," the one year/three year rule should govern Section 10(b) claims. *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1392 (7th Cir. 1990) (emphasis in original), petition for cert. pending, 59 U.S.L.W. 3354 (U.S. Sept. 26, 1990) (No. 90-526).

ARGUMENT

CLAIMS UNDER SECTION 10(b) AND RULE 10b-5 SHOULD BE GOVERNED BY THE ONE YEAR/THREE YEAR STATUTE OF LIMITATIONS THAT THE 73rd CONGRESS PRESCRIBED FOR EXPRESS CAUSES OF ACTION IT CREATED CONTEMPORANEOUSLY WITH THE ENACTMENT OF SECTION 10(b)

Selecting the limitations period applicable to a cause of action created by a federal statute is an inquiry that turns entirely on the intent of the Congress that adopted the statute. The fact that a cause of action is implied rather than express does not shift the focus of the inquiry away from congressional intent. Implied actions are created by Congress, not the courts: a court's conclusion that it should recognize an implied cause of action rests on the court's determination that Congress intended to create that cause of action. See *Thompson* v. *Thompson*, 484 U.S. 174, 179 (1988). Just as congressional intent controls the question whether such a cause of action should be implied in the first place, it controls questions regarding the scope of that action, such as the governing statute of limitations.

When Congress fails to supply an express statute of limitations for a cause of action, and there is no direct evidence concerning the limitations rule that Congress intended to apply, this Court has " 'generally concluded that Congress intended that the courts apply the most closely analogous statute of limitations under state law.' " *Reed* v. *United Transportation Union*, 488 U.S. 319, 323 (1989) (quoting *DelCostello* v. *International Brotherhood of Teamsters*, 462 U.S. 151, 158 (1983)). But this approach to determining congressional intent is not absolute. "[O]n the assumption that Congress would not choose 'to adopt state [limitations] rules at odds with the purpose or operation of federal substantive law,' [the Court has] recognized a closely circumscribed exception

to the general rule that statutes of limitations are to be borrowed from state law." *Reed*, 488 U.S. at 324 (citation omitted). State limitations rules will not apply "when a rule from elsewhere in *federal* law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking." *DelCostello*, 462 U.S. at 172 (emphasis added).

Of course, the general rule favoring application of the "most closely analogous" state statute of limitations—and the accompanying standard for determining when that practice should be discarded—serve only as "a sort of fallback rule of thumb" to fill the gap resulting from the absence of direct evidence of the intent of the Congress that created the cause of action. *DelCostello*, 462 U.S. at 158 n.12; see also *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S. 143, 147 (1987). There is no need for a court to determine which statute of limitations is "most closely analogous"—and undertake the weighing of "federal policies" and "the practicalities of litigation" necessary to make that judgment—if Congress itself identified the appropriate limitations rule. Indeed, rigid adherence to the practice of borrowing from state law could frustrate congressional intent by imposing a statute of limitations different from the one Congress would have intended to apply.[1]

[1] Furthermore, where the cause of action is implied rather than express and the statute contains an analogous express cause of action bounded by an express limitations period, there is considerably less justification for inferring from congressional silence an inclination to adopt state law limitations rules. *United Parcel Service, Inc.* v. *Mitchell*, 451 U.S. 56, 68 n.4 (1981) (Stewart, J., concurring in the judgment); see also *DelCostello*, 462 U.S. at 159 n.12 (reserving question). Because Congress omitted from the statute all reference to the cause of action, its silence regarding the appropriate statute of limitations is not probative. Indeed, the most logical assumption, especially where the implied and express causes of action are closely related, is that Congress would have intended the express statute of limitations to extend to any implied cause of action as well.

There is no need for recourse to the general rule and related inquiries in this case because Congress's intent regarding the appropriate statute of limitations for Section 10(b) claims is clear. Examination of the statute's language, structure, and legislative history establishes that the 73rd Congress, which enacted Section 10(b) in 1934, would have intended that any private action implied under Section 10(b) be governed by the statute of limitations that it prescribed for virtually all of the express causes of action enacted in the Securities Exchange Act of 1934 and the Securities Act of 1933. "It would indeed be anomalous to impute to Congress an intention to expand * * * a judicially implied cause of action beyond the bounds it delineated for comparable express causes of action." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 736 (1975). Accordingly, that is the limitations rule that should be recognized by this Court.

Even if the Court were to apply the analysis it utilizes where there is no direct evidence of congressional intent, moreover, it would reach the same conclusion. The Section 10(b) implied action is unlike any claim under state law, and most closely resembles the express causes of action subject to the limitations rule adopted in the 1934 Act. The relevant policies also weigh strongly in favor of that limitations rule.

A. The 73rd Congress Would Have Intended That Any Implied Cause Of Action Be Governed By The One Year/Three Year Limitations Rule.

The language and legislative history of the 1934 Act leave no doubt regarding the statute of limitations that the 73rd Congress would have applied to the cause of action implied under Section 10(b). The express private causes of action created by the 73rd Congress in the 1934 Act—and the express private causes of action in the 1933 Act—are accompanied by express statutes of limitations. For actions like the one implied under Section 10(b) that require proof of culpability, Congress established the same limitations period: suit must be brought within one

year after discovery of the facts constituting the violation but no later than three years after the transaction in question. 15 U.S.C. §§ 77m, 78i(e), 78r(c); see also *id.* § 78cc(b). That is the rule that should apply to actions under Section 10(b).[2]

First, Section 10(b) claims are closely related—indeed, frequently identical—to the claims that may be brought under the express causes of action. Section 10(b) bars the use "in connection with the purchase or sale of any security * * * [of] any manipulative or deceptive device or contrivance" in contravention of rules adopted by the Securities and Exchange Commission. Rule 10b-5 promulgated thereunder implements this prohibition by forbidding the use in connection with the purchase or sale of securities of (1) "any device, scheme, or artifice to defraud"; (2) "any untrue statement of a material fact or [failure] to state a material fact necessary in order to make the statements made * * * not misleading"; and (3) "any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person." The focus of the statute and the rule is thus the

[2] The only express cause of action in the 1934 Act with a different limitations provision is Section 16(b), 15 U.S.C. § 78p(b), which provides for recovery of profits from "short-swing" transactions in company stock (purchases and sales within a six-month period) by corporate insiders. That cause of action, which is governed by a two-year statute of limitations, differs substantially from Section 10(b) and the other express causes of action under the securities laws. Section 16(b) "is not a disclosure section"; "[n]o proof is required of any misleading representation or omission, or of any statement at all; indeed, not even the most complete disclosure is a defense against recovery of short-swing profits." *Ceres Partners* v. *GEL Associates*, No. 89-7666, slip op. 7270 (2d Cir. Nov. 8, 1990). Section 16(b) is a strict liability provision. *Kern County Land Co.* v. *Occidental Petroleum Corp.*, 411 U.S. 582, 595 (1973). Because Section 16(b) establishes a prophylactic rule for which proof of culpability is not required, courts have agreed that its somewhat shorter statute of limitations is not relevant in determining the proper limitations period for Section 10(b) claims. *Ceres Partners*, slip op. 7270-7271; *In re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1546 (3d Cir.) (en banc), cert. denied, 488 U.S. 849 (1988).

use of deception or any other fraudulent device in connection with securities transactions.

The express causes of action target precisely the same type of conduct. Indeed, claims that may be asserted under these provisions frequently are cast as violations of Section 10(b). For example, Section 9(e) of the 1934 Act, 15 U.S.C. § 78i(e), provides a cause of action for manipulative marketing of securities, including inducing transactions by means of false or misleading statements. The very same conduct may, of course, give rise to a claim under Section 10(b). *Ceres Partners* v. *GEL Associates*, No. 89-7666, slip op. 7267-7268 (2d Cir. Nov. 8, 1990). Section 18 of the 1934 Act, 15 U.S.C. § 78r, allows a purchaser of securities to recover for reliance on false or misleading statements in documents filed with the Commission. "Such a purchaser could instead pursue this type of claim under § 10(b)." *Ceres Partners*, slip op. 7267.

Similarly, Section 11 of the 1933 Act, 15 U.S.C. § 77k, imposes liability for false statements in a registration statement filed with the Commission. Again, where a plaintiff can allege the other elements of a Section 10(b) claim, including trading in reliance on such false information and scienter, he may assert a claim under the latter provision as well. *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 380-387 (1983) (discussing overlap between the two provisions).

Finally, Section 12(2) of the 1933 Act, 15 U.S.C. § 77*l*, provides a remedy for purchasers of securities damaged by false statements made by persons selling the securities. Although Section 10(b) is somewhat broader in scope than Section 12(2), there is a close resemblance in the type of conduct prohibited by the two provisions. As one court has observed, Section 12(2) "describes the offense to which Rule 10b-5 is applied: fraudulent misstatements or omissions in connection with the purchase or sale of securities." *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1390 (7th Cir. 1990), petition for cert.

pending, 59 U.S.L.W. 3354 (U.S. Sept. 26, 1990) (No. 90-526).[3]

Beyond this striking similarity in the conduct covered by the express causes of action and the Section 10(b) implied action, an additional factor—common purpose—also supports the conclusion that the 73rd Congress would have applied an identical limitations period. "Both section 10(b) and its companion provisions * * * are aimed at the same objectives * * *: 'to "provide full and fair disclosure of the character of securities sold in interstate and foreign commerce and through the mails, and to prevent frauds in the sale thereof, and for other purposes."'" *In re Data Access Systems Securities Litigation*, 843 F.2d 1537, 1548 (3d Cir.) (en banc), cert. denied, 488 U.S. 849 (1988) (quoting *Blue Chip Stamps*, 421 U.S. at 728). "All," moreover, "aim to compensate the same type of injury. All are designed to fill a void in the common law and to create remedies that would be uniform throughout our nation's commercial universe." *Data Access*, 843 F.2d at 1548-1549. Accord, *Ceres Partners*, slip op. 7266-7267, 7270.[4]

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[3] Section 29(b) of the 1934 Act, 15 U.S.C. § 78cc(b), provides a cause of action for rescission of certain contracts that violate the Act. It was originally enacted without an express limitations provision but Congress in 1938 amended the provision to impose the one year/three year rule. See Act of June 25, 1938, ch. 677, § 3, 52 Stat. 1076. Because Section 29(b) provides a remedy for violations of any of the substantive provisions of the statute, it plainly overlaps to a considerable degree with the claims that may be asserted under Section 10(b).

[4] The express causes of action cannot be distinguished on the ground that they require a lesser showing of culpability. Although negligence is sufficient for the imposition of liability under some of the express causes of action, proof of scienter is required to prevail under Section 9(e). See, *e.g.*, *Crane Co.* v. *Westinghouse Air Brake Co.*, 419 F.2d 787, 794 (2d Cir. 1969), cert. denied, 400 U.S. 822 (1970). Because Congress did not distinguish among the express causes of action by reference to level of culpability, it would not have distinguished Section 10(b) on the basis of the latter provision's scienter requirement. Indeed, as we discuss below, the legislative history makes clear that Congress specifically intended the one year/three year rule to apply to fraud claims.

In view of the similarity in the types of conduct targeted by the express actions and Section 10(b), the provisions' often-parallel language, and their identical purpose, can there be any doubt what the 73rd Congress would have done if it had anticipated in 1934 that an action would be implied under Section 10(b)? That Congress obviously would have subjected Section 10(b) claims to the limitations rule it applied to the closely-related express actions.

Where, as here, the proper interpretation of a statute is clear from its language and structure, that is where the inquiry should end. *United States* v. *Ron Pair Enterprises, Inc.*, 489 U.S. 235, 240-241 (1989); *Davis* v. *Michigan Dep't of Treasury*, 109 S. Ct. 1500, 1504 n.3 (1989); *Pennsylvania* v. *Union Gas Co.*, 109 S. Ct. 2273, 2296 (1989) (Scalia, J., concurring in part and dissenting in part). Even if recourse to the legislative history of the 1934 Act were appropriate, moreover, the outcome would not change because the legislative history confirms that the 73rd Congress's rationale for adopting the one year/three year limitations rule applies with equal force to Section 10(b) claims.

Congress in 1934 devoted considerable attention to fixing the appropriate statute of limitations. The legislative history reveals that Congress's decision rested on two key determinations. First, too long a period for filing suit would allow a potential plaintiff to wait and see how the security did in the market, thereby speculating at the risk of the alleged wrongdoer:

> [I]f a man buys something today and discovers tomorrow that some mistake has been made and perhaps he has a ground for suit because of fraud, under the terms of the bill he must bring his suit within 1 year. But suppose he thinks, "Perhaps the

> bonds I have bought will go up. I will not bring suit until I find out about that. If the bonds go down then I will have the option of suing these people and trying to recover. If the bonds go up, then I will not sue because I can get a profit on them."

78 Cong. Rec. 8199 (daily ed. May 7, 1934) (statement of Sen. Kean). The one year rule was specifically designed to prevent such speculation.[5]

Congress expressly concluded—after heated debate (78 Cong. Rec. 8198-8203 (daily ed. May 7, 1934))—that one year from discovery provided sufficient time for potential plaintiffs to assert claims grounded in fraud:

> [T]he thought was that a man ought not to delay suit more than 1 year after he discovers the fraud. If he has been injured and finds that he has been injured, he ought to bring his action within a reasonable time, and we fix that time at 1 year.

Id. at 8198 (statement of Sen. Fletcher) (commenting on amendment to reduce the period for filing suit from two

[5] Testimony during the hearings emphasized that the danger of speculation by potential plaintiffs would be enhanced by a longer limitations period. See *Stock Exchange Practices: Hearings on S. Res. 84, S. Res. 56, and S. Res. 97 Before the Sen. Comm. on Banking and Currency*, 73d Cong., 1st Sess. 6910 (1934) (statement of president of the Association of Stock Exchange Firms); *Stock Exchange Regulation: Hearing on H.R. 7852 and H.R. 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 303, 307 (1934) (same).

The Seventh Circuit has more recently reaffirmed the danger of a lengthy limitations period:

> Prices of securities are volatile. If suit may be postponed indefinitely on equitable grounds, then investors may gamble with other people's money. An investor * * * may sell her shares for a price certain. If the firm does poorly, she keeps the money; if it does well, she sues and asks for the increase in value. Congress chose one year after discovery, and a cap of two additional years on tolling principles, in order to curtail the extent to which the securities laws permit recoveries based on the wisdom given by hindsight.

Short, 908 F.2d at 1392.

years to one year). Several Senators objected on the ground that one year was too short a time in which to require potential plaintiffs to file suit. *Id.* at 8199, 8200-8201 (remarks of Sen. Norris); *id.* at 8200 (remarks of Sen. Adams). But the one-year rule was ultimately adopted. See *id.* at 8203.

Second, "Congress included statutes of repose because of fear that lingering liabilities would disrupt normal business and facilitate false claims." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987); see also *Data Access*, 843 F.2d at 1546. The outside time limit on the filing of lawsuits was deemed necessary both to prevent speculation by potential plaintiffs and to provide finality to business transactions. Congress concluded that even a person who could be sued for fraud "ought to feel safe at some reasonable time that he will not be disturbed." 78 Cong. Rec. 8198 (daily ed. May 7, 1934) (remarks of Sen. Fletcher). Congress also feared that permitting plaintiffs to bring suit long after the underlying violation would deter individuals from serving on boards of directors. "Looking at the matter from the standpoint of the director of a corporation, one [consideration] was that we should bring to an end his fear, or the fear of his estate, of a suit." *Id.* at 8200 (remarks of Sen. Byrnes).

One Senator stated that allowing suit within several years of the discovery of the fraud, without an outside limit on the time for filing suit, would give rise to "blackmail." "They discover it after the market has gone down, and after something has happened, and they are looking for mistakes, and years afterwards there is a liability that carries to your grandchildren and great-grandchildren." *Stock Exchange Practices: Hearings on S. Res. 84, S. Res. 56, and S. Res. 97 Before the Sen. Comm. on Banking and Currency*, 73d Cong., 1st Sess. 6565 (1934) (remarks of Sen. Kean).

The conference committee modified the Senate provision, which had fixed the limitations period at one year from discovery but no later than five years after the violation, adopting the one year/three year provision embodied in the final bill. H.R. Conf. Rep. No. 1838, 73d Cong., 2d Sess. 32, 36, 42 (1934). Significantly, the 1934 Act also amended the 1933 Act's limitations provision, substituting the one year/three year rule for the two year/ten year provision originally included in that statute. H.R. Conf. Rep. No. 1838, *supra*, at 42. The one year/three year rule thus embodied Congress's considered judgment concerning the appropriate statute of limitations for virtually all private actions under the 1933 and 1934 Acts.[6]

The debate on the statute of limitations issue—and the essentially universal application of the one year/three year rule—leaves no doubt that Congress would have applied the same limitations rule to actions under Section 10(b). Congress's view of the question did not turn on the specifics of the particular cause of action. Rather, Congress made a generic determination regarding the appropriate statute of limitations for claims under the securities laws, after a debate that centered on the proper rule for "fraud" claims. See generally 78 Cong. Rec. 8198-8201 (daily ed. May 7, 1934). That determination plainly encompasses Section 10(b).

Indeed, applying a different statute of limitations would undercut the policy choice that Congress made with respect to the express causes of action. Because claims brought under the express causes of action frequently may be recharacterized as claims under Section 10(b), a longer limitations period for Section 10(b) would allow

[6] Significantly, Congress in 1938 applied the one year/three year rule to claims under Section 29(b). See page 10, note 3, *supra*. Although Congress did not record the reasons for this action, the most logical deduction is that Congress viewed that limitations rule as the one generally appropriate for private actions under the securities laws.

a plaintiff to circumvent the one year/three year rule by bringing his claim under Section 10(b). The Congress that so carefully chose the one year/three year rule plainly would have prevented that result by applying the same limitations rule to Section 10(b) claims. That is how this Court should construe the statute. *Blue Chip Stamps*, 421 U.S. at 736 (refusing to attribute to Congress the intent to expand Section 10(b) beyond the bounds of the analogous express causes of action); cf. *McAllister* v. *Magnolia Petroleum Co.*, 357 U.S. 221, 226 (1958) (holding that the express statute of limitations governing a Jones Act claim should extend to the parallel admiralty law claim because applying a different rule would undercut the congressional judgment reflected in the express limitations provision).

In sum, the 73rd Congress plainly adopted the one year/three year rule as a general limitations rule for private actions under the provisions of the federal securities laws that provide remedies for "fraud." In these circumstances, "it would seem bizarre if not anomalous to go beyond the express statutes of limitations contained in provisions of the 1934 Act" to find the limitations provision applicable to Section 10(b) actions. *Data Access*, 843 F.2d at 1549. The only logical conclusion is that the one year/three year statute of limitations governs those actions.

The Solicitor General has suggested that the intent of the 73rd Congress is irrelevant in determining the proper limitations period because Congress did not contemplate an implied cause of action under Section 10(b) and could not have foreseen the growth in the scope of that cause of action. U.S. Am. Br. at 17-18, *Lebman* v. *Aktiebolaget Electrolux*, cert. denied, 109 S. Ct. 3214 (1989). But the fact that the courts may have erred in recognizing the implied Section 10(b) action in the absence of any evidence that Congress intended that result (see page 5, *supra*) provides no justification for compounding

the damage by ignoring the evident intent of the 73rd Congress in ascertaining the appropriate statute of limitations. Rather, that fact provides an additional reason for hewing to clear congressional intent with respect to the scope of the implied action.

Thus, the Court has looked to congressional intent, as expressed in the words of the statute and the legislative history, in shaping the Section 10(b) action. *Blue Chip Stamps*, 421 U.S. at 731-736; see also *id.* at 755 (Powell, J., concurring) ("emphasiz[ing] the significance of the texts of the Acts of 1933 and 1934"). The Court did state in *Blue Chip Stamps* that Congress had not "foreordained the present state of the law with respect to Rule 10b-5"; the Court therefore weighed several "policy considerations" in determining how to "flesh out the portions of the law with respect to which neither the congressional enactment nor the administrative regulations offer conclusive guidance." *Id.* at 737. Here, however, as we have discussed, the congressional enactment *does* offer conclusive guidance. The Court should vindicate Congress's intent by holding that Section 10(b) actions are governed by the one year/three year rule.[7]

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[7] Congress's inaction in the face of the lower courts' failure to apply the one year/three year rule does not somehow erase the intent of the 73rd Congress, as the Solicitor General suggested in his *Lebman* brief (at 18 n.22). This Court in *Malley-Duff* held a federal limitations period applicable to civil RICO actions despite congressional inaction in the face of adoption of various state limitations periods by the lower courts. Indeed, the Court rejected the argument for congressional ratification in *Malley-Duff* even though Congress had specifically considered amendments to RICO that would have established a federal limitations period. 483 U.S. at 154-155.

B. Application Of The Test Utilized In *DelCostello*, *Malley-Duff*, And *Reed* Confirms That Section 10(b) Claims Should Be Governed By The One Year/Three Year Rule.

In view of Congress's clear intent to adopt the one year/three year rule as an across-the-board statute of limitations for securities law claims, there is no need for recourse to the test that applies when Congress has not spoken regarding the governing limitations rule. See pages 5-6, *supra*. Should the Court nonetheless find it appropriate to undertake the latter inquiry, the Court should first consider whether all claims under Section 10(b) should be characterized the same way or the limitations rule should differ depending on the nature of the claim. Next, the Court should identify the cause of action most analogous to Section 10(b). Because the express actions subject to the one year/three year statute of limitations bear a strikingly close resemblance to suits under Section 10(b), that limitations rule should apply to Section 10(b) actions.

1. *The Statute Of Limitations Applicable To A Section 10(b) Claim Should Not Vary Depending On The Factual Basis Of The Claim.*

The initial inquiry in determining the appropriate statute of limitations is "whether all claims arising out of the federal statute 'should be characterized in the same way, or whether they should be evaluated differently depending upon the varying factual circumstances and legal theories presented in each individual case.'" *Malley-Duff*, 483 U.S. at 147 (quoting *Wilson* v. *Garcia*, 471 U.S. 261, 268 (1985)); see also *Reed*, 488 U.S. at 325. This Court has found in a variety of statutory contexts that a uniform limitations rule is necessary to avoid uncertainty and wasteful litigation. See *Reed*, 488 U.S. at 326; *Malley-Duff*, 483 U.S. at 149-150; *Wilson*, 471 U.S. at 275. That determination is also true with respect to Section 10(b).

Section 10(b), like the RICO statute and 42 U.S.C. § 1983, "encompass[es] numerous and diverse topics and subtopics." *Wilson*, 471 U.S. at 273; see also *Malley-Duff*, 483 U.S. at 149-150. Claims may be brought by a purchaser or seller of securities against "*any* person" who engages in conduct prohibited by Section 10(b). Defendants may include securities issuers, officers and directors, underwriters, accountants, lawyers, traders in the securities markets, and broker-dealers. Claims may be premised on misrepresentations in documents filed with the Commission, false public statements by the issuer, manipulation of securities markets, trading on inside information, and overreaching by broker-dealers.[8] The statute truly "embrace[s] a galaxy of actions." *Data Access*, 843 F.2d at 1543.

Moreover, each of these claims may be characterized in different ways; for example, as fraud, breach of fiduciary duty, breach of contract, or a violation of a state statute such as a blue sky law. "If the choice of the statute of limitations were to depend upon the particular facts or the precise legal theory of each claim, counsel could almost always argue, with considerable force, that two or more periods of limitations should apply to each [Section 10(b)] claim." *Wilson*, 471 U.S. at 274.

The resulting uncertainty about the applicable statute of limitations has real adverse consequences. Plaintiffs may be misled as to the deadline for filing their claims and defendants " 'cannot calculate their contingent liabilities, not knowing with confidence when their delicts lie in repose.' " *Malley-Duff*, 483 U.S. at 150 (quoting *Wilson*, 471 U.S. at 275 n.34). In addition, resources are diverted into unnecessary collateral litigation over the

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[8] See, *e.g.*, *Basic Inc.* v. *Levinson*, 485 U.S. 224 (1988); *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299 (1985); *Herman & MacLean, supra; Santa Fe Industries, Inc.* v. *Green*, 430 U.S. 462, 476-477 (1977); *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128 (1972).

proper limitations rule. Accordingly, there can be no doubt that for Section 10(b) a "uniform statute of limitations is required to avoid intolerable 'uncertainty and time-consuming litigation.' " *Malley-Duff*, 483 U.S. at 150 (quoting *Wilson*, 471 U.S. at 272). See also *Data Access*, 843 F.2d at 1540-1541, 1543-1544 (outlining complexity of "matching" particular types of Section 10(b) claims with different statutes of limitations and rejecting that approach in favor of a single limitations rule).

2. *Section 10(b) Claims Should Be Subject To A Uniform Federal Limitations Rule.*

The uniform limitations period for Section 10(b) claims should be drawn from federal rather than state law. First, as we have discussed (see pages 8-10, *supra*), federal securities law contains statutory provisions that closely resemble Section 10(b). The state law analogies, by contrast, do not adequately capture the multifaceted nature of Section 10(b). For example, this Court has recognized that "[a]ctions under Rule 10b-5 are distinct from common-law deceit and misrepresentation claims." *Basic Inc.* v. *Levinson*, 485 U.S. 224, 244 n.22 (1988). See also *Blue Chip Stamps*, 421 U.S. at 744-745 ("the typical fact situation in which the classic tort of misrepresentation and deceit evolved was light years away from the world of commercial transactions to which Rule 10b-5 is applicable"). Common law fraud actions thus are not sufficiently analogous to Section 10(b) actions to justify the borrowing of state statutes of limitations applicable to fraud claims. *Ceres Partners*, slip op. 7264-7265; *Data Access*, 843 F.2d at 1544-1545.

Analogies to other state law claims are similarly defective. See *Data Access*, 843 F.2d at 1543-1544, 1549 (flaws in analogy to state blue sky laws). The variety of different state law analogies adopted by the courts of appeals—including fraud actions, blue sky claims, and

personal injury actions[9]—itself demonstrates that no single state law action is truly analogous to Section 10(b) claims.

Second, Section 10(b) actions, like civil actions under RICO, "involve interstate transactions." *Malley-Duff*, 483 U.S. at 153. Indeed, a nexus with interstate commerce is a necessary prerequisite for claims under RICO and Section 10(b) alike. Accordingly, the "multistate nature of" Section 10(b) claims strongly "indicates the desirability of a uniform federal statute of limitations." *Malley-Duff*, 483 U.S. at 154. See also *Ceres Partners*, slip op. 7250 ("federal securities regulation is inherently national in scope and in need of uniform rules").[10]

Parties to a single transaction frequently are scattered across the country. In the interest of fundamental fairness and certainty for all concerned, a "broker in Phoenix, an issuer in San Francisco, a purchaser in Montana, an accountant in Portland, and a lawyer in Honolulu should be subject to the same statute of limitations for actions based on Section 10(b) or Rule 10b-5." *Davis* v. *Birr, Wilson & Co.*, 839 F.2d 1369, 1375 (9th Cir. 1988) (Aldisert, J., concurring); accord, *Data Access*, 843 F.2d at 1549. Otherwise, "if two suits are brought in different states seeking damages for a single act in violation of the federal securities laws, one suit may be barred

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[9] See U.S. Am Br. App., *Lebman* v. *Aktiebolaget Electrolux*, *supra*.

[10] "This is in marked contrast to the typical § 1983 suit, in which there need not be any nexus to interstate commerce, and which most commonly involves a dispute wholly within one State." *Malley-Duff*, 483 U.S. at 154. See *Wilson*, *supra* (applying state personal injury limitations statutes for § 1983 claims); *Reed*, 488 U.S. at 325-327 (applying state personal injury statute of limitations to claim that union violated officer's free speech rights under the Labor-Management Reporting and Disclosure Act, relying on close similarity between the LMRDA and § 1983 actions).

while the other is not." *Ceres Partners*, slip op. 7253.[11] There is simply no reason that the viability of federal law claims asserted by identically-situated plaintiffs should turn upon the state in which the lawsuits are filed or the plaintiffs reside. ABA, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 647 (1986) ("*ABA Report*"). As this Court recently observed in *Reves* v. *Ernst & Young*, 110 S. Ct. 945, 954 (1990), Congress did not "intend[] the Securities Acts to apply differently to the same transactions depending on the accident of which State's law happens to apply."

Third, there are compelling practical justifications for applying a uniform federal limitations rule to Section 10(b) claims. "[T]he use of state statutes * * * present[s] the danger of forum shopping." *Malley-Duff*, 483 U.S. at 154; L. Loss, *Fundamentals of Securities Regulation* 993 (2d ed. 1988). Around the country, statutes of limitations for claims under Section 10(b) vary widely, ranging from as little as one year in Maryland to as much as six years in Michigan. *ABA Report* at 663, 664. With so wide a disparity, the temptation to shop for the most generous limitations period is overwhelming, "especially under a statute like the 1934 Act [see 15 U.S.C. § 78aa] that provides for a broad choice of venue and nationwide service of process." Loss, *supra*, at 993.

In addition, precious judicial resources are wasted determining the appropriate statute of limitations. *ABA*

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[11] The Second Circuit cited one Section 10(b) action in which *twenty-six* separate statutes of limitations had been applied. *Ceres Partners*, slip op. 7253 (citing *Kronfeld* v. *Advest, Inc.*, 675 F. Supp. 1449, 1457-1458 & n.21 (S.D.N.Y. 1987)). "Indeed, there is no theoretical reason that residents of all 50 states could not be joined in a single suit or represented in a class action, with the result that more than 50 not-particularly-appropriate state statutes could provide the sources for determining whether the respective claims of otherwise identically situated plaintiffs were time-barred." *Ceres Partners*, slip op. 7266.

Report at 647; Loss, *supra*, at 994. The uncertainty and unpredictability caused by application of federal tolling rules to state statutes of limitations, which may incorporate tolling rules of their own, exacerbate this problem. "Deciding which features of state periods of limitation to adopt for which federal statutes wastes untold hours. Never has the process been more enervating than in securities law. There are many potentially analogous state statutes, with variations for different kinds of securities offenses and different circumstances that might toll the period of limitations. Both the bar and scholars * * * have pleaded, with a unanimity rare in the law, for help." *Norris*, 818 F.2d at 1332 (citation omitted). See also *ABA Report* at 654-655.[12]

All relevant factors thus point sharply in favor of a uniform federal rule. Indeed, that is the virtually unanimous conclusion reached by the commentators that have addressed the issue.[13]

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[12] The uncertainty that necessarily results from reliance on state limitations rules is most vividly illustrated by two recent Fifth Circuit decisions in a single case. The court first held the plaintiffs' Section 10(b) claim time barred, applying the Texas statute of limitations for fraud actions. On rehearing, the court vacated its prior opinion because Texas had lengthened its fraud statute of limitations from two years to four years and the plaintiffs' claims were viable under the new limitations rule. *In re Sioux, Ltd., Securities Litigation*, 901 F.2d 51, 52-53, vacated, 914 F.2d 61, 63-64 (5th Cir. 1990).

[13] See, *e.g.*, *ABA Report* at 657-658; Loss, *supra*, at 995; Ruder, *Civil Liability Under Rule 10b-5: Judicial Revision of Legislative Intent?*, 57 Nw. U.L. Rev. 627, 649-650, 681 n.243 (1962) (the author was chairman of the SEC from 1987 to 1989); A. Bromberg, *Securities Law: Fraud: SEC Rule 10b-5* § 12.9, at 284 (1967); Israels, Book Review, 77 Yale L.J. 1585, 1591-1592 (1968); Block & Barton, *Statute of Limitations in Private Actions Under Section 10(b)—A Proposal for Achieving Uniformity*, 7 Sec. Reg. L.J. 374, 381-382 (1980); Bloomenthal, *Statutes of Limitations and the Securities Acts—Part II*, 7 Sec. & Fed. Corp. L. Rep. (Clark Boardman) 25, 25-26, 30 (Apr. 1985).

3. *The Causes Of Action Subject To The One Year/Three Year Rule Provide The Closest Analogy To Section 10(b) Claims.*

Every court of appeals to hold that a uniform federal statute of limitations should govern Section 10(b) actions has chosen the one year/three year rule. *Ceres Partners*, slip op. 7266-7274; *Short*, 908 F.2d at 1390-1392; *Data Access*, 843 F.2d at 1549. The other possibility, a rather recent entry, is part of a new express cause of action for insider trading that was added to the 1934 Act by the Insider Trading and Securities Fraud Enforcement Act of 1988 (ITSFEA). This new action, codified as Section 20A of the 1934 Act, 15 U.S.C. § 78t-1, imposes liability on "[a]ny person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information." 15 U.S.C. § 78t-1(a). Section 20A(b) limits this cause of action in several ways, and includes a statute of limitations providing that "[n]o action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation." 15 U.S.C. § 78t-1(b)(4).

To begin with, it is highly questionable whether the new five year limitations period should even be considered as a possible statute of limitations for Section 10(b) actions. The five year rule was enacted 54 years after Section 10(b). Certainly, the 73rd Congress could not have contemplated application of that limitations rule. This distinguishes the present situation from *Malley-Duff*, where the Court applied the Clayton Act statute of limitations to RICO actions in part because RICO's legislative history indicated that Congress might have intended that result. 483 U.S. at 150-152. And in *DelCostello*, the federal limitations rule that the Court applied to the federal claims was enacted in the same statute as those causes of action. 462 U.S. at 169.

Giving consideration to any statute of limitations that happens to be in the United States Code on the day that

the question is presented to a court for decision, no matter what the date of that statute's adoption, leads to very anomalous results. For example, when the Third Circuit decided *Data Access*, Section 20A had not yet been enacted. Assuming that the court correctly concluded that a federal statute of limitations should apply to Section 10(b) actions, the one year/three year rule was the only provision available. What position would the Solicitor General have taken if the Court had invited the views of the United States in *Data Access*? Was that decision correct when rendered, but now erroneous due to the subsequent enactment of Section 20A?

Indeed, "[a]ny court choosing a federal statute of limitations between 1946 (the date of the first decision recognizing a private right of action under Rule 10b-5) and 1988 necessarily would have selected" the one year/three year rule. *Short*, 908 F.2d at 1390. What if five courts of appeals had reached that conclusion; would they all be required to reexamine their prior decisions on the ground that Section 20A is a better "fit"? And what if Congress in 1992 adds a new express cause of action to the securities laws with a two year/four year statute of limitations; will the lower courts—and eventually this Court—have to consider again which is the most appropriate limitations rule for Section 10(b)?

The possibilities are endless, but the point is obvious: an open-ended inquiry leads neither to certainty nor finality. A court always will have to reconsider, and possibly alter, its decision in the event a new federal statute of limitations is enacted.

" 'Few areas of the law stand in greater need of firmly defined, easily applied rules than does the subject of periods of limitations.' " *Wilson*, 471 U.S. at 266 (quoting *Chardon* v. *Fumero Soto*, 462 U.S. 650, 667 (1983) (Rehnquist, J., dissenting)). The Court may for that reason wish to limit the potential "candidates" to those limitations provisions already in existence on the date of

enactment of the statute giving rise to the cause of action and those limitations rules adopted concurrently with that statute. If Congress wishes to create a new statute of limitations for an already-existing cause of action, it would of course remain free to do so by legislation.

At the very least, the Court should view with extreme skepticism suggestions to apply federal statutes of limitations enacted long after the substantive provision in question. Especially where, as here, a clearly appropriate statute of limitations existed at the time Congress enacted the substantive statute, the Court should not expand the inquiry unnecessarily.

Assuming, *arguendo*, that Section 20A is eligible for consideration, the Court should nonetheless apply the one year/three year rule to Section 10(b) actions. The express causes of action that are limited by the one year/three year rule supply the "closest analog[ies]" to Section 10(b). *Malley-Duff*, 483 U.S. at 150.

First, Section 20A's five year limitations rule does not by its terms apply to Section 10(b) actions. Indeed, Congress intended that this provision *not* alter development of the law regarding Section 10(b). See 15 U.S.C. § 78t-1(d) ("[n]othing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this chapter or the availability of any cause of action implied from a provision of this chapter").

Second, Section 10(b) is much more analogous to the causes of action subject to the one year/three year rule than it is to Section 20A. We have already discussed the close similarities between these provisions with respect to the conduct prohibited, their parallel language, and their identical purpose. See pages 8-10, *supra*. To be sure, Section 20A resembles the other express causes of action under the securities laws in that it encompasses conduct that also is actionable under Section 10(b). But Section 20A "focuses only on insider trading. * * *

Th[e] section has no relationship to any of the many other types of claims that can be maintained under" Section 10(b). *Ceres Partners*, slip op. 7271. For example, allegations of express misrepresentations, omissions of material information, and other forms of fraud, which serve as the basis for the vast majority of the claims brought under Section 10(b)—and which are actionable under the express causes of action subject to the one year/three year rule—are not covered by Section 20A. Because it singles out only one "particular and atypical kind of violation" (*Short*, 908 F.2d at 1392), Section 20A's narrow focus contrasts sharply with the variety of claims that may be asserted under the other express actions and Section 10(b).

Moreover, Congress crafted Section 20A with reference to considerations unique to the insider trading context. The statute was "one of 'a variety of measures designed to provide greater deterrence, detection and punishment for violations of insider trading.' These measures were needed because of the difficulties of ferreting out evidence sufficient to prosecute insider trading cases." *Ceres Partners*, slip op. 7271 (quoting H.R. Rep. No. 910, 100th Cong., 2d Sess. 7 (1988)). Thus, the evolution of the five year statute of limitations makes clear that the provision represents Congress's judgment about the appropriate statute of limitations for *insider trading* offenses, not for other types of securities law violations.

The provision was drawn from the Insider Trading Sanctions Act of 1984, which authorizes the Securities and Exchange Commission to seek civil penalties against inside traders; this penalty authority is limited by a five year statute of limitations. See 15 U.S.C. § 78u-1 (d)(5).[14] Congress simply adopted the same five year

[14] That limitations period, in turn, was based on the statute of limitations for criminal prosecutions under the 1934 Act. *The Insider Trading Act of 1983: Hearing on H.R. 559 Before the Subcomm. on Securities of the House Comm. on Banking, Housing, and Urban Affairs*, 98th Cong., 2d Sess. 28 (1984) (statement of SEC Chairman Shad).

rule for the new private cause of action for insider trading created by Section 20A. *The Insider Trading Proscription Act of 1987: Hearing on S. 1380 Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs*, 100th Cong., 1st Sess. 30 (1987) (SEC proposed bill); see also *Definition of Insider Trading: Hearings Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing, and Urban Affairs*, 100th Cong., 1st Sess., pt. 1, at 40 (1987) (joint statement of Harvey L. Pitt and John F. Olson). The provision thus originated as a limitation on the general rule that the SEC's enforcement authority is not restricted by *any* statute of limitations. It would be peculiar indeed to borrow from a provision intended to *circumscribe* the SEC's authority in order to *expand* the rights of private litigants bringing claims that Congress did not even consider at the time it enacted the five year provision.

The one year/three year rule, by contrast, was specifically intended by Congress to serve as a *general* statute of limitations for *private* actions seeking recovery for violations of the securities laws. See pages 14-15, *supra*. It is "the statute *designed for* the kind of conduct about which * * * most * * * 10b-5 plaintiffs complain." *Short*, 908 F.2d at 1392 (emphasis in original). That generic judgment, rather than Congress's determination that "unique measures were necessary to curb insider trading," should apply to Section 10(b) actions. *Ceres Partners*, slip op. 7272. Indeed, because Congress in 1934 expressly rejected a five year limitations rule on the ground that it was too long (see page 14, *supra*), this Court should be especially reluctant to extend the Section 20A limitations provision beyond the insider trading context.[15]

[15] The policy judgments made by Congress in 1934—that one year leaves a plaintiff sufficient time to file a claim, that a statute of repose is necessary to ensure certainty in business affairs, and that longer time periods would encourage speculation by potential

Third, it is not clear whether the five year limitations period is a statute of repose, cutting off claims five years from the date of the underlying conduct, or whether the five year period is subject to equitable tolling. See *Short*, 908 F.2d at 1392. As we have discussed, "[s]etting an outer limit for claiming fraud or material omissions in the sale of securities is an important aspect of [the one year/three year rule], one of the principal reasons Congress designed the statute that way." *Ibid.* This uncertainty regarding the parameters of the five year rule weighs strongly against applying that rule to Section 10(b) claims. *Id.* at 1392.

Finally, the practicalities of litigation do not favor a different result. Section 20A is an *additional* remedy for insider trading; it does not supplant the remedy now provided by Section 10(b). Insider trading plaintiffs will presumably assert claims under both Section 10(b) and Section 20A, just as plaintiffs claiming injury from, for example, market manipulation, bring parallel claims under Sections 9 and 10(b). See, *e.g.*, *Schaefer* v. *First National Bank*, 509 F.2d 1287, 1292-1293 (7th Cir. 1975), cert. denied, 425 U.S. 943 (1976). And, because Section 20A and the other express causes of action are subject to different statutes of limitations, complete consistency is impossible: the limitations rule for Section 10(b) actions necessarily will be different from the rule governing some express action. That inconsistency will be minimized if Section 10(b) actions are subject to the

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plaintiffs (see pages 11-13, *supra*)—remain valid today. As one court has observed, these considerations may weigh differently with respect to insider trading because the potential damages award "is fixed within days after the trading, sometimes within hours. * * * [N]o one can use delay in bringing suit to speculate on the firm's future prosperity." *Short*, 908 F.2d at 1392. The enactment of the five year period for insider trading actions accordingly does not undercut Congress's earlier judgment with respect to the generality of securities fraud actions.

rule applicable to most express actions—the one year/three year rule.

To be sure, a plaintiff whose claims are untimely under the one year/three year rule might try to characterize them as insider trading allegations in order to obtain the benefit of the longer statute of limitations. But Section 20A plainly has no application to the whole spectrum of Section 10(b) claims asserted against nontrading defendants. "In the great bulk of cases, there will be no ambiguity." *Short*, 908 F.2d at 1391. Moreover, Section 20A's less generous damages rule, which limits damages to the defendant's "profit gained or loss avoided" less any amount disgorged to the SEC (15 U.S.C. § 78t-1(b)(1) & (2)), provides a significant disincentive to such chicanery.

In sum, every relevant factor establishes that the one year/three year rule represents Congress's judgment concerning the appropriate limitations period for the broad spectrum of securities fraud encompassed by Section 10(b). This Court should hold that rule applicable to Section 10(b) actions.[16]

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[16] Respondents stated in their brief in opposition (at 10) that in the event the Court granted certiorari, "whether the statute of limitations should be changed retroactively to bar respondents' fraud claims will be a major issue." Five Justices recently indicated that decisions in civil cases generally apply retroactively. See *American Trucking Ass'ns, Inc.* v. *Smith*, 110 S. Ct. 2323, 2347-2352 (1990) (Stevens, J., dissenting, joined by Brennan, Marshall, and Blackmun, JJ.); *id.* at 2343-2345 (Scalia, J., concurring in the judgment). Even if the retroactivity question turns on the factors identified by the Court in *Chevron Oil Co.* v. *Huson*, 404 U.S. 97 (1971), moreover, this Court can and should decide the statute of limitations issue on the merits before proceeding to the question of retroactivity. *Id.* at 100-105; cf. *United States* v. *Leon*, 468 U.S. 897, 924-925 (1984). Indeed, the Court may leave the question of retroactivity to be determined on remand.

CONCLUSION

The judgment of the court of appeals should be reversed.

Respectfully submitted.

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Respondents.

On Writ of Certiorari to the United States
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BRIEF OF SECURITIES INDUSTRY ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF PETITIONER

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No. 90-333

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BRIEF OF SECURITIES INDUSTRY ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF PETITIONER

Preliminary Statement

Pursuant to Rule 37 of this Court and with consent of the parties, the Securities Industry Association ("SIA") submits this brief as amicus curiae in support of Petitioner.[1]

This case presents important issues not previously considered by the Court concerning the appropriate statute of limitations to govern judicially implied causes of action under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b), and Rule 10b-5

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[1] Written consents signed by all parties have been filed with the Clerk's office.

thereunder, 17 C.F.R. 240.10b-5. The principal issue is whether the limitations period for 10b-5 actions should be borrowed from an analogous state statute, as the court below concluded, or whether 10b-5 claims should be governed by the federal limitations period applicable to virtually all of the express causes of action under the federal securities laws — one year from the date of discovery but in no event longer than three years from the violation.

A further issue, which was not raised below but which we believe may be presented by the Securities and Exchange Commission as amicus curiae, is whether the five-year statute of limitations applicable to actions under the Insider Trading and Securities Fraud Enforcement Act of 1988, 15 U.S.C. § 78t-1 ("ITSFEA"), is a better federal alternative than the one-year/three-year limitations period.

Interest of Amicus Curiae

The Securities Industry Association is the principal trade association of the securities industry. Its members include approximately six hundred securities firms in the United States and Canada. Its membership is responsible for over ninety percent of the securities business conducted in this country. SIA's members serve securities investors of every size and type and perform the complete spectrum of professional securities activities, including retail and institutional brokerage, over-the-counter market-making, underwriting and other investment banking activities, money management, and investment advisory services.

SIA is generally recognized as a spokesman for the securities industry in general and the broker-dealer community in particular. A major function of SIA is to address legislative and regulatory matters affecting the securities industry on the national and state levels.

SIA has a substantial interest in this Court's determination of the limitations period applicable to 10b-5 actions. The current practice of borrowing variant state limitations periods makes it impossible for securities professionals to determine their rights with any degree of certainty. Moreover, tremendous expense is incurred by SIA members in litigation over the choice of an appropriate state limitations period.

The adoption of a uniform federal rule will remove the uncertainty and needless expense that has long haunted the securities industry in 10b-5 litigation.

SIA is also concerned with the SEC's proposal that the five-year ITSFEA limitations period be adopted for 10b-5 actions rather than the one-year/three-year rule. Longer limitations periods severely prejudice defendants by forcing them to litigate stale claims where memories are fuzzy and evidence is lost or misplaced. Protracted periods of potential exposure also make it easier for plaintiffs to speculate at the risk of the seller of securities by waiting to see if the market causes the securities to increase or decrease in value. The legislative history of the 1934 enactments clearly reflects a Congressional preference for a limitations period that balances the competing considerations of investor protection on the one hand with prompt and certain resolution of securities disputes on the other. The one-year/three-year scheme was specifically designed to fulfill these objectives; the five-year insider trading provision was not.

SUMMARY OF ARGUMENT

Because private actions under Rule 10b-5 are a judicial creation, there is no express statute of limitations for such claims. Accordingly, federal courts must "absorb" a statute of limitations for Rule 10b-5 from elsewhere in the law. Until recently, most courts routinely borrowed an analogous state limitations period. This practice has produced chaos. The use of variant state limitations periods creates differing time limits for similarly situated individuals asserting the same federal cause of action, encourages forum shopping, fosters expensive and unnecessary litigation, and runs directly counter to express Congressional intent to create a uniform, federal system of securities litigation and to assure a period of repose against stale claims. Almost unanimously, commentators have condemned the use of state law and have advocated adoption of a uniform federal statute of limitations.

In *DelCostello v. International Brotherhood of Teamsters*, 462 U.S. 151, 172 (1983), and *Agency Holding Corp. v. Malley-Duff & Associates*, 483 U.S. 143, 148 (1987), the Court held that a federal claim that lacks a statute of limitations should be governed by a federal limitations period if it provides "a closer analogy than available state statutes" and if "the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking." The one-year/three-year limitations period applicable to virtually all express claims under the federal securities laws satisfies this standard. Section 10(b) and the express causes of action governed by the one-year/three-year rule are part of the same legislative scheme, created by Congress at the same time, with the same objectives, to remedy the same types of injury. Additionally, application of a federal limitations period provides for uniformity and certainty, eliminates forum shopping, avoids expensive litigation and more closely reflects Congressional intent. To date three circuits have adopted this federal rule for 10b-5 actions. *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.) (en banc), *cert. denied*, 488 U.S. 849 (1988); *Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990), *petition for cert. filed*, 59 U.S.L.W. 3278 (U.S.

September 26, 1990) (No. 90-526); *Ceres Partners v. GEL Associates*, __ F.2d __, No. 89-7666 (2d Cir. Nov. 8, 1990) (1990 WL 171509).[2]

The one-year/three-year provision is a far better federal alternative than the five-year limitations period found in ITSFEA. The express causes of action created in the 1933 and 1934 enactments bear a much closer similarity in purpose and structure to Rule 10b-5 than does the atypical violation prohibited by ITSFEA. Moreover, the one-year/three-year rule reflects deliberate and careful balancing by Congress of the competing policies of investor protection and repose.

In contrast, the five-year limitations period in ITSFEA reflects no balancing whatsoever of the competing interests but was simply copied from the limitations provision contained in a predecessor statute which, in turn, was drawn from the criminal catchall statute of limitations. No court has adopted the ITSFEA five-year provision and the only two appellate courts that have considered this alternative (*Short* and *Ceres*) have rejected it.

[2] Those circuits declining to adopt a federal limitations period, including the Ninth Circuit, have done so solely on the basis of *stare decisis* rather than as a result of considered analysis of the alternatives. *See* discussion, *post*, at 13.

ARGUMENT

RULE 10B-5 CLAIMS SHOULD BE GOVERNED BY THE STATUTE OF LIMITATIONS IMPOSED ON EXPRESS CAUSES OF ACTION UNDER THE FEDERAL SECURITIES LAWS, WHICH REQUIRES THAT AN ACTION MUST BE BROUGHT WITHIN ONE YEAR OF DISCOVERY AND WITHIN THREE YEARS OF THE VIOLATION.

When Congress enacted the Securities Exchange Act of 1934, it created, along with Section 10(b), several express private rights of action. *See* § 9(e), 15 U.S.C. § 78i(e) (manipulation of security prices); §18(c), 15 U.S.C. § 78r(c) (liability for misleading statements in any application, report, or filed document); § 29(b), 15 U.S.C. § 78cc(b) (voiding contracts in violation of the Act) (added in 1938). Each of these express, Congressionally-ordained causes of action carries a limitations period of one year from the date of discovery and a maximum of three years from the date of the violation. Section 9(e), 15 U.S.C. § 78i(e), is typical: "No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation."[3]

At the same time that Congress passed the original 1934 Act, it also reduced the limitations period applicable to claims under the Securities Act of 1933 to conform with the one-year/three-year scheme being imbedded into the 1934 Act. *See* 15 U.S.C. § 77m. The original prescriptive period for private actions under the 1933 Act had been two years from the date of discovery but no more than ten years from the date of the violation. *See* 48 Stat. 84 (1933).

No statute of limitations was provided for Section 10(b) claims because Congress did not create any private cause of action under that

[3] Section 16(b) of the 1934 Act, 15 U.S.C. § 78p(b), sets a two-year period for initiating litigation. Section 16(b) is a strict liability provision under which an insider's short-swing profits can be recovered by the corporation regardless of the intent or knowledge of the insider, and is thus readily distinguishable from the other provisions of the Act. *See* discussion in *Ceres*, WL 171509 at 15.

provision. Such a right is, in the words of Judge Aldisert, "a genie sired solely by the judiciary." *Data Access*, 843 F.2d at 1547. *See Superintendent of Insurance v. Bankers Life & Casualty Co.*, 404 U.S. 6, 13 n.9 (1971) ("It is now established that a private right of action is implied under 10(b)"). The question thus presented is what limitations period is most appropriate for this "genie" extrapolated from the 1934 Act.

A. The Court Should Apply a Uniform Federal Limitations Period to 10b-5 Actions Rather than Borrowing State Law.

Until recently, most courts borrowed a limitations period found in an analogous state statute. This practice has resulted in a body of law as confused and unwieldy as any developed in the federal courts. Different limitations periods ranging anywhere from one to six years can apply to similarly situated parties asserting the very same federal cause of action. *Compare Data Controls North, Inc. v. Financial Corp. of America, Inc.*, 688 F.Supp. 1047, 1050 (D. Md. 1988), *aff'd mem.*, 875 F.2d 314 (4th Cir. 1989) (using Maryland's one-year blue sky statute of limitations) *with Mercer v. Jaffe, Snider, Raitt & Heuer*, 713 F.Supp. 1019, 1026 (W.D. Mich. 1989) (applying Michigan's six-year limitations period for fraud). Even within a given circuit, limitations periods vary substantially in length and courts borrow different types of statutes in different states. *Compare Shelter Mutual Ins. Co. v. Public Water Supply Dist. No. 7*, 569 F.Supp. 310, 312 (E.D. Mo. 1983), *aff'd*, 747 F.2d 1195 (8th Cir. 1984) (utilizing Missouri's two-year blue sky statutory limitations period) *with Rude v. Campbell Square, Inc.*, 411 F.Supp. 1040, 1048 (D.S.D. 1976) (borrowing South Dakota's six-year limitations period for common-law fraud). Forum shopping is thus encouraged as plaintiffs search for the states with the most lenient time requirements. Defendants have no way of predicting which rule will govern a particular dispute until an action is actually filed and a forum determined.

Predictability is further hindered by application of the doctrine of "equitable tolling," which means that the state's limitations period may not begin to run until the date when the wrongdoing is actually

discovered or "should have been" discovered. *See, e.g., Vanderboom v. Sexton*, 422 F.2d 1233, 1240 (8th Cir.), *cert. denied*, 400 U.S. 852 (1970). The uncertainty created by equitable tolling also significantly diminishes the likelihood of a disposition of the limitations issue on summary judgment and provides lower courts, like the Ninth Circuit here, an opportunity to implement their antiquated philosophy that "summary disposition on the ground of the statute of limitations is discouraged." (Slip op. at 4.)

The state-law borrowing approach is most unpredictable where the plaintiffs reside in several different states, as is often the situation in consolidated or class actions. Even though all claims may spring from the same operative facts, courts will frequently apply a different limitations period to each plaintiff, with the indefensible result that the claims of some plaintiffs may be time-barred while those of others are not. *See, e.g., Kronfeld v. Advest, Inc.*, 675 F.Supp. 1449, 1457-58 & n.21 (S.D.N.Y. 1987) (district court applied 26 separate statutes of limitations); *In re National Student Marketing Litigation*, Fed. Sec. L. Rep. ¶ 97,926 (D.D.C. March 26, 1981) (noting possible applicability of 34 different states' statutes of limitation in class action). *See Ceres*, WL 171509 at 3 ("Indeed, there is no theoretical reason that residents of all 50 states could not be joined in a single suit or represented in a class action, with the result that more than 50 not-particularly-appropriate state statutes could provide the sources for determining whether the respective claims of otherwise identically situated plaintiffs were time-barred").

Other courts choose a single limitations period, drawn from the state with the "most significant contacts" to the action, and apply it to all class members. *State Teachers Retirement Board v. Fluor Corp.*, 80 F.R.D. 142, 145 (S.D.N.Y. 1978). At least one court has eschewed logic in favor of simplicity by using the statute of limitations of the forum state for all class members — even while admitting that this produces the "inconceivable" result of reviving the "dead and breathless" claims of non-resident class members who would have been barred had they brought suit in their home state. *Pinney v. Edward D. Jones & Co.*, 735 F.Supp. 915, 917 (W.D. Ark. 1990), *interlocutory appeal pending*, No. 90-1680WA (8th Cir.).

Courts and commentators alike have condemned the current state of the law. In 1986 a special Task Force of the American Bar Association studying limitations periods for 10b-5 actions summarized the prevailing view:

> "Such disarray serves no public purpose. This uncertainty and lack of uniformity promote forum shopping by plaintiffs and result in wholly unjustified disparities in the rights of parties litigating identical claims in different states. Neither plaintiffs nor defendants can determine their rights with any certainty. Vast amounts of judicial time and attorneys' fees are wasted."

Report of the Task Force on Statute of Limitations for Implied Actions, 41 BUS. LAW. 645, 647 (1986) ("ABA Task Force Report"). Judge Easterbrook colorfully referred to this situation as "one tottering parapet of a ramshackle edifice." *Norris v. Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), *cert. denied*, 484 U.S. 943 (1987). One district judge more bluntly described it as an area of law that "simply 'makes no sense.' " *Pinney v. Edward D. Jones & Co.*, 915 F.Supp. at 916.

Regrettably, the chaos that has resulted was totally avoidable. Courts just as easily could have chosen a uniform federal limitations statute, drawn from Section 10(b)'s sister provisions in the 1933 and 1934 Acts, to govern 10b-5 actions. As Justice Brennan pointed out in his concurring opinion in *McAllister v. Magnolia Petroleum Co.*, 357 U.S. 221, 228-29 (1958), the rationale of early Court decisions sanctioning the use of state limitations periods was not that state statutes should automatically be used, but rather that where a state statute *is the only one available*, the choice is between a state limitations period and none at all:

> "[T]he considerations which in *Campbell v. Haverhill*, [155 U.S. 610 (1895)] and *Cope v. Anderson*, [331 U.S. 461 (1947)] prompted resort to the state statutes do not apply at all here. Those cases represented intensely practical solutions to a practical problem in the administration of justice. *In the absence of any comparable federal statute of limitations* which might be applied, the Court had four choices: (1) No period of limitations

at all; (2) an arbitrary period applicable in all like cases; (3) the flexible but uncertain doctrine of laches; and (4) state statutes of limitations. *The state statutes were chosen by default.*"[4]

Until recently, the federal option for 10b-5 actions was not utilized. Instead, aided by counsel's failure to urge otherwise, lower courts automatically used state limitations periods. "Federal courts are so accustomed to turning to state periods of limitations that we (and our colleagues in other circuits) did this on auto-pilot, without discussing whether something differentiated securities laws from other statutes." *Short*, 908 F.2d at 1387.

The consensus among courts and commentators is that the practice of borrowing state limitations periods for 10b-5 actions was a mistake. "[T]he courts missed a turn. Courts should have drawn the periods of limitations for the implied rights from the periods of limitations for the express rights." *Norris v. Wirtz*, 818 F.2d at 1333. *See also* Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5*, 1972 DUKE L.J. 1125, 1149 (1972) (the practice of borrowing state limitations periods for 10b-5 actions "must be judged as a mistake in application of principle"); Bloomenthal, *The Statute of Limitations and Rule 10b-5 Claims: A Study in Judicial Lassitude*, 60 U. COLO. L. REV. 235, 236 (1989) ("The history of this judicial travesty is replete with evidence of sloppy scholarship, the willingness of the courts to accept *dicta* without analysis, and the remarkable inefficiency of the federal judicial system in resolving disputed issues of federal law").

In *DelCostello* the Court finally put to rest the notion that federal courts were somehow "bound" by state law in determining the appropriate limitations period for federal claims. The Court held that a federal statute of limitations, § 10(b) of the NLRA, 29 U.S.C. § 160(b), should apply to hybrid duty-of-fair-representation claims under § 301 of the NLRA, which lacks an express limitations period. The Court noted that the choice of a time limit for a federal cause of action "is

[4] Emphasis ours here and throughout this brief except where otherwise noted. In *McAllister* the Court adopted a federal statute of limitations, applying a prescriptive period from the Jones Act to an action under maritime law to recover for unseaworthiness. *Id.* at 224.

itself a question of federal law," 462 U.S. at 159 n.13, and that state statutes of limitations are useful merely as a convenient method of "fashioning remedial details where Congress has not spoken," not because state law somehow controls. *Id.* at 159. The Court explained that federal courts have *always* been free to borrow federal limitations periods:

> "[W]hen a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking, *we have not hesitated to turn away from state law*." *Id.* at 172.

The Court illustrated its point by reference to past cases such as *McAllister*, *Holmberg v. Armbrecht*, 327 U.S. 392 (1946), and *Occidental Life Insurance Co. v. EEOC*, 432 U.S. 355 (1977), in which it declined to borrow state statutes. 462 U.S. at 162-63.

In *Agency Holding Corp. v. Malley-Duff & Associates*, 483 U.S. 143 (1987), the *DelCostello* rationale was applied to determine the appropriate prescriptive period for civil actions brought pursuant to the Racketeer Influenced and Corrupt Organizations Act ("RICO"), 18 U.S.C. § 1964, which includes an express provision for civil liability but does not contain a limitations period. The Court was presented with an array of conflicting viewpoints akin to that which currently exists with respect to 10b-5 actions: federal judges had "not adopted a consistent approach to the problem of selecting the most appropriate statute of limitations," *id.* at 148; lower courts had "uniformly looked to state statutes of limitations," *id.* at 149; and commentators had lamented that the law was "confused, inconsistent and unpredictable." *Id.* at 148.

Agency Holding reaffirmed the appropriateness of borrowing federal limitations periods: "Although it has been suggested that federal courts always should apply the state statute of limitations most analogous to each individual case whenever a federal statute is silent on the proper limitations period, a clear majority of the Court rejected such a single path." *Id.* at 146 (citations omitted). Because of "the

similarities in purpose and structure between RICO and the Clayton Act [and] the clear legislative intent to pattern RICO's civil enforcement provision on the Clayton Act," *id.* at 152, the Clayton Act was deemed "a far closer analogy than any available state statute." *Id.* at 156. The Court also determined — in language especially apposite here — that the "federal policies at stake and the practicalities of litigation" strongly favored application of a federal rule:

> "As this case itself illustrates, RICO cases commonly involve interstate transactions, and conceivably the statute of limitations of several states could govern any given RICO claim. Indeed, some nexus to interstate or foreign commerce is required as a jurisdictional element of a civil RICO claim. . . . The multistate nature of RICO indicates the desirability of a uniform federal statute of limitations. With the possibility of multiple state limitations, the use of state statutes would present the danger of forum shopping and, at the very least, would 'virtually guarante[e] . . . complex and expensive litigation over what should be a straightforward matter.' "*Id.* at 153-54.

Following *Agency Holding*, three Courts of Appeals have abandoned the historical practice of borrowing state limitations periods for 10b-5 actions and have adopted the one-year/three-year rule applicable to most express causes of action under the federal securities laws. The Third Circuit in *Data Access* was the first to utilize the federal rule, followed by the Seventh Circuit in *Short* and the Second Circuit in *Ceres*.[5] The Eighth Circuit has stayed consideration of the issue pending the Court's decision in this case. *Pinney v. Edward D. Jones & Co.*, No. 90-1680WA (8th Cir. October 23, 1990). Two district courts have adopted the one-year/three-year federal scheme without waiting for authority from the circuit. *Robertson v. Deloitte, Haskins & Sells*, 732 F.Supp. 979, 985 (E.D. Ark. 1990); *Welch v. Cadre Capital*, 735 F.Supp. 467, 481-82 (D. Conn. 1989).

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[5] *Data Access* was an *en banc* decision. The opinion in *Short* was circulated to all judges in active service in the circuit and no judge voted to hear the case *en banc*. 908 F.2d at 1389. The *Ceres* opinion was also circulated to all active circuit judges. WL 171509 at 18.

Many of the lower federal courts that have declined to adopt a uniform limitations period, including the court below, have done so on the basis that they felt hemmed-in by circuit precedent. *See, e.g., Smith v. Duff & Phelps, Inc.*, 891 F.2d 1567, 1570 (11th Cir. 1990) ("one panel of the Court is not permitted to overrule a decision by a previous panel unless the Court overrules the earlier decision by an en banc proceeding"); *Bath v. Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817, 819 (10th Cir. 1990) ("district court is bound to follow the precedent of this circuit, regardless of its views concerning the advantages of the precedent of our sister circuits"); *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990) (declining to follow *Data Access* without consideration *en banc*).

The reasons supporting the adoption of a federal limitations period for 10b-5 actions are unassailable. The express causes of action created by Congress under the same statutory scheme provide a "far closer analogy," *Agency Holding*, 483 U.S. at 156, to Section 10(b) than any state alternatives. Judically-implied 10b-5 claims and the legislatively-created claims spring from the same common origin with the same objectives, to remedy the same type of injury. Section 10(b) was not just "patterned after" the express causes of action, *cf. Agency Holding*, 483 U.S. at 156; it was created as part of the very same legislation. It is hard to imagine a more "analogous" cause of action. *Cf. Blue Chip Stamps v. Manor Drug Stores*, 421 U.S 723, 741 (1975) (choices made by Congress with respect to the express terms written into the federal securities acts are entitled to great weight in fashioning the scope of remedies for implied actions under Section 10(b)).

The only reasonable interpretation of Congressional intent is that if Congress had created a private right to sue under Section 10(b), it would have used the same limitations period that it appended to the express causes of action that are part of the same legislative scheme. "Congress has spoken directly to the appropriate statute of limitations for [10b-5] litigation. . . ." *Short*, 908 F.2d at 1388. "Given Congress' enactment of specific periods of limitation for every private right of action that it expressly provided in the federal securities laws, we conclude that judicial selection of a uniform nationwide limitations

period is what Congress would have intended for private rights of action judicially implied under those laws." *Ceres*, WL 171509 at 3.

A federal limitations period better effectuates the federal policies at stake. The federal securities laws were enacted precisely because the securities markets were national in scope and no single state's laws were capable of regulating the nation's capital markets. *See* 15 U.S.C. § 78b ("[T]ransactions in securities as commonly conducted upon securities exchanges and over-the-counter markets *are affected with a national public interest* which makes it necessary to provide for regulation and control of such transactions and of practices and matters related thereto. . . .") Application of differing limitations periods to similarly situated parties asserting the same right runs counter to this goal of federal uniformity. *Cf. Reves v. Ernst & Young*, __ U.S. __, 110 S.Ct. 945, 954 (1990) ("We are unpersuaded that Congress intended the Securities Acts to apply differently to the same transactions depending on the accident of which State's law happens to apply").

The use of diverse state limitations periods, coupled with application of the equitable tolling doctrine, frustrates the strong federal policy favoring repose of securities claims at a predictable time. The legislative history from 1934 reflects that certainty of repose against stale claims was one of the overriding concerns of Congress when it enacted the Exchange Act. *See Norris v. Wirtz*, 818 F.2d at 1332 ("The legislative history in 1934 makes it pellucid that Congress included statutes of repose because of fear that lingering liabilities would disrupt normal business and facilitate false claims"). Application of the one-year/three-year federal limitations period will ensure certainty as Congress intended.

The "practicalities of litigation" persuasively counsel against resort to state limitations periods for 10b-5 actions. The state-law borrowing approach plainly encourages forum shopping, a practice long disfavored by this Court. Moreover, since interstate commerce is a jurisdictional predicate for the application of Rule 10b-5, resort to state law virtually guarantees complex and expensive litigation over the choice of a limitations period. Adoption of a single federal statute of limitations will put an end to the inefficiency and chaos that has plagued courts and parties alike.

B. The One-Year/Three-Year Rule Is the Most Appropriate Federal Statute of Limitations To Govern Implied Private Rights of Action Under Section 10(b) of the 1934 Act.

The Securities and Exchange Commission agrees that adoption of a uniform federal limitations period for 10b-5 actions is preferable to the practice of borrowing state limitations periods. But the SEC has contended that a different federal limitations period — the five-year rule governing the insider trading prohibition in ITSFEA, 15 U.S.C. § 78t-1 — should be selected by the Court.[6] This alternative has not been adopted by any court and has been rejected by both Courts of Appeals that have considered the issue. *Short*, 908 F.2d at 1392; *Ceres*, WL 171509 at 6.

The express claims in the '33 and '34 Acts are much closer to Rule 10b-5 in "purpose and structure," *Agency Holding*, 483 U.S. at 152, than are ITSFEA claims. There is substantial overlap between the conduct covered by the express actions and that covered by implied actions under Rule 10b-5. *See Ceres*, WL 171509 at 14 (noting that Rule 10b-5 overlaps §§ 9(e) and 18(a) of the '34 Act and § 11 of the '33 Act); *Short*, 908 F.2d at 1390-91 (§§ 11 and 12 of the '33 Act cover the same offenses as § 10(b)). Indeed, Section 10(b) was purposely designed by Congress as a broad "catchall" category that would provide statutory authority for the Commission to add to the list of prohibited or regulated practices that were not specifically enumerated in other sections of the Acts. *See Stock Exchange Regulation: Hearings on H. R. 7852 and H. R. 8720 Before the House Comm. on Interstate and Foreign Commerce*, 73d Cong., 2d Sess. 115 (1934), *reprinted in* 8 J. Ellenberger & E. Mahar, *Legislative History of the*

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[6] The SEC took this position in an amicus curiae brief filed in *Lebman v. Aktiebolaget Electrolux*, (U.S., No. 88-1114). *See* Brief for the United States as Amicus Curiae, filed June 6, 1989. The brief was submitted at the Court's request in connection with a petition for certiorari in *Lebman v. Aktiebolaget Electrolux*, 854 F.2d 1319 (5th Cir. 1988). Certiorari was eventually denied in *Lebman*, 109 S. Ct. 3214 (1989). We expect the SEC to take the same position in this case, although to date it has declined to reveal its intentions in this regard.

Securities Act of 1933 and Securities Exchange Act of 1934 (1973) (original section 9(c), which eventually became Section 10(b), "is a catchall clause to prevent manipulative devices .... The Commission should have the authority to deal with new manipulative devices"); *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 206 (1976) ("the catchall provision of § 10(b)" should be interpreted in accordance with the elements of an action under Section 9 of the '34 Act).

In contrast to the kinship between Rule 10b-5 and its sister provisions in the '33 and '34 Acts, ITSFEA is directed at an "atypical kind of violation." *Short*, 908 F.2d at 1392. It applies only to "purchasing or selling a security while in possession of material, nonpublic information" and affords a remedy solely to persons who "contemporaneously" purchased or sold "securities of the same class." 15 U.S.C. § 78t-1(a). Damages are limited to the wrongdoers' profit, § 78t-1(b)(1), rather than the plaintiffs' loss. The victims of this unique offense are usually strangers to the illicit conduct who are unaware that a violation has even occurred. Consideration of these factors led Judge Easterbrook in *Short* to reject the ITSFEA five-year rule for 10b-5 cases:

> "To select § 20A(b)(4) as the rule for *all* Rule 10b-5 actions, just because a five-year period has been deemed appropriate for one atypical kind of violation, would let the tail wag the dog. Congress did not say that § 20A applies to all cases under Rule 10b-5; it did not amend § 13 [of the 1933 Act, specifying a one-year/three-year period]; it limited the scope of § 20A(b)(4)'s statute of limitations to a particular and atypical kind of violation. Section 20A(b)(4) has been prescribed for inside trading cases; run-of-the-mine frauds under Rule 10b-5 should be governed by the statute in force when Rule 10b-5 came into being, the statute *designed for* the kind of conduct about which Short and most other 10b-5 plaintiffs complain: § 13 of the Securities Act of 1933." 908 F.2d at 1392 (emphasis in original).[7]

In *DelCostello*, 462 U.S. at 169, the Court recognized that the ultimate objective is to utilize that limitations period which is "actually designed to accommodate a balance of interests . . . similar to that at stake" for the federal claim at issue. The one-year/three-year rule fulfills this objective. The legislative history of the 1934 enactments reflects that this provision was the result of a deliberate attempt by Congress to "accommodate a balance" between investor protection and repose in securities fraud actions. Before they arrived at the present rule, Congress debated a host of other limitations schemes: two years from discovery with no cutoff; two years from discovery with a six-year maximum; no longer than two years from the violation; and no longer than three years from the violation.[8] *See also* Schulman,

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[7] If the goal is to select the limitations period that requires the shortest "leap into the realm of legislative judgments," as Justice Scalia suggested in his dissent in *Agency Holding*, 483 U.S. at 157, then the one-year/three-year rule is clearly a better choice than the five-year ITSFEA provision. Adoption of a limitations period that was enacted as part of the very same legislation as Section 10(b) plainly requires less of a legislative-type judgment by the judiciary than selection of a limitations period created more than fifty years later for a unique species of securities fraud.

[8] When the 1934 Act was initially introduced, the precursors to what eventually became Sections 9(e) and 18 contained a limitations period of two years from discovery of the violation, and no outer limit. S. 2693, 73d Cong., 2d Sess. §§ 8(e), 17(e) (1934), *reprinted in* 11 J. Ellenberger & E. Mahar, Item 34 at 20, 33; H.R. 7852, 73d Cong., 2d Sess. §§ 8(e), 17(e) (1934), *reprinted in* 10 J. Ellenberger & E. Mahar, Item 24 at 20, 33. A six-year maximum was added to the version of the bill that was reported out of the Senate Committee on Banking and Currency. S. 3420, 73d Cong., 2d Sess. §§ 9(e), 18(c) (1934), *reprinted in* 11 J. Ellenberger & E. Mahar, Item 37 at 23, 41. Thereafter, Senator Fletcher, the Chairman of the Senate Committee on Banking and Currency, introduced the "Fletcher Amendments" to the 1933 Act, which, as passed by the Senate, reduced the limitations periods in that Act from the initial two-year/ten-year formulation to one year from discovery and five years from the violation, and also amended the limitations period in the proposed 1934 Act to conform to the new, lower one-year/five-year limitations periods being proposed for actions under the 1933 Act. *See* 11 J.

(Footnote 8 continued on next page)

Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion, 13 WAYNE L. REV. 635, 637 (1967) (statute of limitations provisions in securities acts were "the subject of deep and perhaps exaggerated congressional interest").

The one-year limitation period beginning with the date of discovery was "thoroughly discussed by the [Senate] committee," 78 CONG. REC. 8198 (1934) (statement of Sen. Walcott), and was characterized by a Senate floor leader and Conference Committee member as the result of an attempt to "agree upon something that would be just and fair to both sides." 78 CONG. REC. 8200 (1934) (statement of Sen. Byrnes). Senator Fletcher, who was chairman of the committee that drafted the Senate version of the bill, floor manager of the measure in the Senate and a member of the Conference Committee, explained that:

> "[T]he thought was that a man ought not to delay suit more than 1 year after he discovers the fraud. If he has been injured and finds that he has been injured, he ought to bring his action within a reasonable time, and we fix that time at 1 year." 78 CONG. REC. 8198 (1934).

(Footnote 8 continued from previous page)

Ellenberger & E. Mahar, Item 38; *see also* 78 CONG. REC. 8198 (1934) (Senator Fletcher explaining purpose of latter amendment to "chang[e] this provision, so as to make it conform to the Securities Act as we will eventually amend that act").

In the meantime, the House version of the 1934 Act had been reintroduced by Representative Rayburn first with a two-year limitations period measured from the date "the cause of action accrued," H.R. 8720, 73d Cong., 2d Sess. §§ 8(d), 17(c) (1934), *reprinted in* 10 J. Ellenberger & E. Mahar, Item 28 at 26, 43, and later containing a three-year absolute limitations period measured from "the violation," H.R. 9323, 73d Cong., 2d Sess. §§ 8(e), 17(c) (1934), *reprinted in* 10 J. Ellenberger & E. Mahar, Item 29 at 24, 40. It initially passed in the House in the latter form, *see* 10 J. Ellenberger & E. Mahar, Item 31. The Conference Committee borrowed a little from each version, applying the Senate's one-year-from-discovery provision and the House's three-year absolute cutoff to actions under Sections 9(e) and 18 of the new 1934 Act and applying them as well to the 1933 Act. H.R. Rep. No. 1838, 73d Cong., 2d Sess. (1934), *reprinted in* 5 J. Ellenberger & E. Mahar, Item 20 at 32,42.

As the Third Circuit noted in *Data Access*, "[a]fter the plaintiff has notice, there is a strong federal interest in requiring him to file suit quickly." 843 F.2d at 1546 (*quoting Roberts v. Magnetic Metals Co.*, 611 F.2d 450, 463 (3d Cir. 1979) (Seitz, C. J. dissenting)). But the five-year ITSFEA provision does not require any diligence upon discovery of the alleged wrongdoing. An investor can wait five years, regardless of when he discovers the alleged fraud, to file suit. The lack of any discovery rule fatally flaws the ITSFEA provision as a limitations period for 10b-5 actions. As Senator Barkley noted in the Senate debate on the '34 Act:

> "By putting in a limitation of 1 year after the discovery of the fraud, we are actually limiting the possibility of litigation . . . . [W]hen we say, 'Although you discovered the fraud within a month or within 6 months after it was committed, you have to bring suit within a year, or you cannot bring it at all,' we actually limit rather than encourage litigation. Otherwise, the man could go on until the end of 5 years, although he had known about the fraud all the time, and still bring his suit." 78 CONG. REC. 8199 (1934).

Cf. Burnett v. New York Central Railroad Co., 380 U.S. 424, 428 (1965) ("the courts ought to be relieved of the burden of trying stale claims when a plaintiff has slept on his rights").

Congress likewise had specific and well-considered reasons for adopting the definitive three-year cutoff. "It was understood that the three-year rule was to be absolute." *Norris*, 818 F.2d at 1332. *See, e.g.*, 78 CONG. REC. 10,186 (1934) (statement of Sen. Byrnes) ("[T]he amendments adopted today [reducing the ten-year absolute cut-off in the 1933 Act to three years] give greater assurance to the honest officials of a corporation . . . ."); 78 CONG. REC. 8198 (1934) (statement of Sen. Fletcher) (A person "ought to feel safe at some reasonable time that he will not be disturbed").

In contrast to the deliberate and careful balancing that went into creation of the one-year/three-year scheme, the ITSFEA five-year rule contained in § 20A(b)(4) reflects no balancing whatsoever of the

competing considerations relevant to securities fraud claims. The five-year provision actually originated in the Insider Trading Sanctions Act of 1984 ("ITSA"), 15 U.S.C. § 78u-1, which expanded the powers of the SEC to act against unlawful insider trading but did not provide for an express private right of action. Because the SEC was empowered to seek treble damages, which could involve potentially staggering sums, a five-year statute of limitations, drawn from the criminal law dealing with securities law violations, was added. *See* H.R. Rep. No. 355, 98th Cong., 2d Sess., *reprinted in* 1984 U.S. CODE CONG. & ADMIN. NEWS 2274, 2302.[9] The intended perimeters of this limitations period were strictly circumscribed. As the legislative history of ITSA explicitly states, "[t]he [five-year] limitation [period] is applicable *solely* to actions brought under this legislation." *Id.* at 2285.

In 1988, in the face of growing insider trading scandals, ITSA was amended and supplemented by ITSFEA, and an express private right of action was created. But *nowhere* in the history of the 1988 legislation is there *any* evidence that *any* consideration was given to the limitations provision, other than a passing, unadorned statement that the five-year period from ITSA would apply to ITSFEA. *See* 133 CONG. REC. S8247 (1987) (statement of Sen. Riegle); H.R. Rep. No. 910, 100th Cong., 2d Sess., *reprinted in* 1988 U.S. CODE CONG. & ADMIN. NEWS 6043, 6076. Thus, the reasons for adopting the five-year limitations period in ITSFEA were not even remotely related to the policy reasons exhaustively discussed by Congress in connection with the express remedies of the '33 and '34 Acts. *Cf. Agency Holding*, 483 U.S. at 155 (five-year federal criminal statute of limitations "does not reflect any congressional balancing of the competing equities unique to civil RICO actions or, indeed, any other federal civil remedy").

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[9] At the hearings on this proposed legislation, John Shad, then Chairman of the SEC, commented: "A five-year statute of limitations for penalty actions was added to the House bill. This conforms to the five-year statute of limitations for criminal violations of the Securities Exchange Act . . . ." *The Insider Trading Sanctions Act of 1983: Hearing on H.R. 559 Before the Subcomm. on Securities of the Senate Comm. on Banking, Housing and Urban Affairs*, 98th Cong., 2d Sess. 28 (1984).

A longer, five-year period may be appropriate for ITSFEA given the "difficulties of ferreting out evidence sufficient to prosecute insider trading cases," *Ceres*, WL 171509 at 15, but it has no application to run-of-the-mill 10b-5 actions. "Prudent investors almost always can sniff out fraud (or enough smoke to justify litigation) within three years. Section 13 cuts off only the claims of the most trusting or somnolent — or the most wily, those who wanted to wait as long as possible." *Short*, 908 F.2d at 1392. As previously discussed, Congress specifically rejected limitations periods longer than three years, including a one-year/five-year limitations scheme, for all other express federal securities claims it created.[10]

Three years is well within the mainstream of legislative judgments concerning the appropriate length of prescriptive periods applicable to securities fraud actions. In addition to the one-year/three-year scheme found in the federal securities acts, the vast majority of the state legislatures have enacted limitary periods of three years or less. *See ABA Task Force Report*, 41 BUS. LAW. at 662-66 (all but seven at time of survey). Moreover, Section 606 of the Uniform Securities Act (1985) recommends application of the same one-year/three-year scheme found in the federal securities laws. The comment to that section indicates that the three-year period was considered to be on the long end of the spectrum: "There appears to be a split among the states today between using a two-year or three-year outside statute of limitation. The Committee opted for the longer three-year limit."

A longer limitations period increases the prejudice to defendants that inheres in stale claims. Securities claims are often "easier to advance than refute," *Norris v. Wirtz*, 818 F.2d at 1333. The longer litigation is delayed, the more difficult it is for a defendant to marshal evidence to defend himself. As this Court stated in *Burnett v. New York Central Railroad Co.*:

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[10] Imposition of an absolute three-year limitations bar on federal claims will not shut out investors who, through no fault of their own, have failed to discover what is genuinely a fraud. Aggrieved parties will still have the full panoply of state common-law claims from which to draw, including common-law fraud.

"Statutes of limitations are primarily designed to assure fairness to defendants. Such statutes 'promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared. The theory is that even if one has a just claim it is unjust not to put the adversary on notice to defend within the period of limitation and that the right to be free of stale claims in time comes to prevail over the right to prosecute them.'" 380 U.S. at 428, *quoting Order of Railroad Telegraphers v. Railway Express Agency, Inc.*, 321 U.S. 342, 348-49 (1944).

The five-year ITSFEA limitations period conflicts with rules promulgated by the SEC governing the length of time that broker-dealers must keep and preserve essential books and records. The vast majority of such records, including those relevant to defense of a 10b-5 claim, are required to be kept no longer than three years. *See* Rules 17a-3 and 17a-4, 17 C.F.R. 240.17a-3 and 17 C.F.R. 240.17a-4. Broker-dealers who justifiably rely on these regulations may be unable to defend themselves properly if investors are allowed to wait five years before bringing suit.

A longer limitation period also makes it easier for a plaintiff to speculate at the risk of the seller of securities. An investor who thinks he has been defrauded can elect to see how his investment turns out before commencing litigation. Obviously, the longer the investor is allowed to wait, the greater the chance that any subsequent loss will be attributable to intervening market forces wholly unrelated to the initial wrongdoing. As the stock market becomes more volatile, the risk of such unforeseeable liability increases drastically. "Congress chose one year after discovery, and a cap of two additional years on tolling principles, in order to curtail the extent to which the securities laws permit recoveries based on the wisdom given by hindsight." *Short*, 908 F.2d at 1392. By contrast, damages under ITSFEA are limited to the profits of the violator and are not affected by subsequent fluctuations in the stock market.

Conclusion

For the reasons stated, the Court should hold that the statute of limitations applicable to judicially implied actions under Rule 10b-5 is the federal rule requiring an action to be brought within one year of discovery of the alleged fraud and in no event later than three years from the violation.

Respectfully submitted,

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In the Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW, PETITIONER

v.

JOHN GILBERTSON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION AS AMICUS CURIAE

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QUESTION PRESENTED

Whether the statute of limitations for implied private actions under the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5, should be drawn from state law or from an express limitations period found in the federal securities laws.

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In the Supreme Court of the United States

OCTOBER TERM, 1990

No. 90-333

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW, PETITIONER

v.

JOHN GILBERTSON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION AS AMICUS CURIAE

INTEREST OF THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission is responsible for the administration and enforcement of the federal securities laws. This case presents the issue whether the statute of limitations for implied private actions under the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934 (Exchange Act or 1934 Act), 15 U.S.C. 78j(b), and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5, should be drawn from state law, or from an express limitations period found in the federal securities laws. Private actions provide " 'a most effective weapon in the enforcement' of the securities laws and are 'a necessary supplement to Commission action.' " *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 310 (1985), quoting *J.I. Case Co.* v. *Borak*, 377 U.S. 426, 432 (1964). The Commission has a strong interest, therefore, in the development of principles governing such private actions that promote, rather than impede, the purposes of the securities laws.

STATEMENT

1. From late 1979 through mid-1981, respondents purchased units in one or more of seven similar limited partnerships. The partnerships bought, and then leased to others, computer hardware and software, and were designed to provide tax advantages for investors. Petitioner is a law firm that helped organize the partnerships and provided legal services, including preparing the tax opinion. Pet. App. 28A-30A.

The partnerships failed. In addition, respondents later learned that they did not realize tax benefits. In 1982 and 1983, respondents were notified that the Internal Revenue Service was investigating the partnerships. Pet. App. 31A-32A. In 1985, according to respondents, fraud was uncovered following the IRS's disallowance of tax benefits because of overvaluation of partnership assets and lack of profit motive. See Resp. C.A. Joint Reply Br. 12-14.

2. On November 3, 1986, respondents filed complaints in the United States District Court for the District of Oregon.[1] The complaints alleged that the offering memoranda misrepresented the tax consequences of the investments, the profitability of the partnerships' business, the marketability of the software, and the accuracy of equipment appraisals, thereby violating, *inter alia*, Section 10(b) of the Exchange Act and Rule 10b-5. Pet. App. 32A-33A.

On petitioner's motion for summary judgment, the district court held that respondents' Section 10(b) claims were barred by the applicable statute of limitations. The court applied Oregon's two-year period governing fraud claims, subject to tolling until the injured party had "actual or inquiry notice" of the facts supporting the complaint. Because the court found that respondents were on inquiry notice of fraud as early as October 1982—more than four years before filing suit—the court concluded that respondents' claims were time-barred. Pet. App. 35A-43A.

[1] On June 4, 1987, a third complaint was filed by respondent Anthony Catalan. The district court consolidated the three actions for discovery and pretrial proceedings. Resp. C.A. Joint Br. 5 n.4.

3. The court of appeals reversed, holding that there were unresolved factual issues regarding when respondents discovered or should have discovered the alleged fraud that precluded summary judgment. Pet. App. 12A-18A. The court thereby rejected petitioner's argument that a federal limitations period, drawn from the Exchange Act, of one year from discovery, but no more than three years from the violation, should apply to Rule 10b-5 claims. See Pet. C.A. Joint Br. 14-16, citing *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.), cert. denied, 488 U.S. 849 (1988). The court concluded that in the Ninth Circuit the "analogous forum state statute of limitations period continues to govern § 10(b) claims." Pet. App. 12A.

SUMMARY OF ARGUMENT

The borrowing of state limitations periods for Section 10(b) and Rule 10b-5 private actions has generated widespread, persistent confusion in the lower courts, and has made litigation under these provisions needlessly complex and unpredictable. Recently, three courts of appeals, inspired by this Court's recent formulation of the analysis for selecting statutes of limitations for federal claims having no express period, have selected a limitations period from federal law. Although we disagree with those courts' selection of the one-and-three-year periods dating from the original securities acts, we agree that a uniform federal period should govern private Section 10(b) actions, and we believe that the five-year statute of limitations contained in Section 20A of the Exchange Act, enacted in the Insider Trading and Securities Fraud Enforcement Act of 1988, best accommodates the competing interests.

A federal limitations period should be borrowed when it governs a claim that is more analogous to the right at issue than is any state claim, and when policy concerns and litigation practicalities make the federal period significantly better for securing the pertinent federal inter-

ests. Section 20A, which codifies a right of action for certain insider trading violations, satisfies those requirements. It represents the only occasion on which Congress has provided an express private right of action for violations of Section 10(b). In taking that step, Congress enacted a statute of limitations of five years from the last transaction that is the subject of the violation. Not only are the elements of a Section 10(b) violation under Section 20A the same as in other Section 10(b) claims, but the policy balance that Congress struck in Section 20A, in establishing the appropriate length of time to sue for certain insider trading violations, readily applies to the general category of violations covered by Section 10(b). Finally, borrowing Section 20A's limitations period promotes the federal interest in uniform and efficient enforcement of the securities laws throughout the Nation.

The competing federal alternative is the one-and-three-year periods provided when Congress enacted the securities laws over half a century ago. Not only do these periods represent a far more remote appraisal of limitations policies, they also apply expressly to rights of action that are not as closely analogous to Section 10(b) as the Section 20A remedy. Moreover, applying the one-and-three-year provisions at this late date would substantially shorten the prevailing limitations periods borrowed from state law and would thereby impair investor protection.

Selecting the one-and-three-year periods would also stimulate new limitations disputes in Section 10(b) litigation, as courts and litigants struggle to determine which of two limitations periods (the five year or the one-and-three year) governs a particular case. The likely proliferation of those disputes runs counter to the very reasons for selecting a uniform federal period for Section 10(b) cases in the first place. Finally, adoption of the Section 20A period is consonant with the consistent theme of the securities laws of ensuring repose at a definite and predictable time, thus guarding against lingering and stale claims.

ARGUMENT

THE STATUTE OF LIMITATIONS GOVERNING RULE 10b-5 PRIVATE ACTIONS SHOULD BE DRAWN FROM THE FIVE-YEAR PERIOD FOUND IN SECTION 20A OF THE SECURITIES EXCHANGE ACT

A. The Traditional Approach of Borrowing State Limitations Periods Under Rule 10b-5 Has Produced Confusing and Inconsistent Results

Congress did not expressly create a private cause of action under Section 10(b); accordingly, there is no express limitations period for implied actions under Rule 10b-5.[2] Until recently, courts faced with limitations questions under Rule 10b-5 routinely turned to the state limitations period governing what was thought to be the most appropriate analogy to the federal claim. This "borrowing" of state law accorded with the traditional practice of looking to the law of the forum state to provide a limitations period for federal claims when federal law is silent on the applicable limitations period. *American Pipe & Constr. Co.* v. *Utah*, 414 U.S. 538, 556 n.27 (1974); *Auto Workers* v. *Hoosier Cardinal Corp.*, 383 U.S. 696, 703-705 (1966); *Holmberg* v. *Armbrecht*, 327 U.S. 392, 395 (1946). On two occasions, this Court noted the prevailing practice under Rule 10b-5 of applying state limitations periods; in neither case did the Court consider the appropriateness of that practice or the practical difficulties it engenders. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 210-211 & n.29 (1976); *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 384 & n.18 (1983).

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[2] See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 196 (1976). Shortly after the Commission adopted Rule 10b-5, a district court held that there was an implied right of action under the Rule. *Kardon* v. *National Gypsum Co.*, 69 F. Supp. 512 (E.D. Pa. 1946). Since that time, an implied right of action under Rule 10b-5 has been uniformly recognized by courts and sanctioned by congressional acquiescence. *Basic Inc.* v. *Levinson*, 485 U.S. 224, 230-231 (1988). The existence of the implied right of action is today "simply beyond peradventure." *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 380-381 & n.10 (1983).

Experience has revealed, however, that the borrowing of state limitations periods for Rule 10b-5 produces confusing and inconsistent results. The resort to state limitations periods requires an assessment of which variety of state claim furnishes the most suitable "analogy" to the Rule 10b-5 claim. Courts have disagreed, however, on the analytical approach to use in searching for the proper analogue.[3] Since there is a wide variety of potentially analogous state law claims, the differing methods for discerning the limitations period have resulted in borrowing several different types of statutes, ranging in length from one to ten years.[4]

Early cases generally applied the periods governing common law fraud.[5] Two courts of appeals continue to

[3] Some courts apply a "substantive resemblance" test, which examines the similarity of the elements of the state and federal claims; other courts apply a "commonality of purpose" test, which examines the similarity of the policies vindicated by the two claims. See generally Note, *Limitation Borrowing in Federal Courts*, 77 Mich. L. Rev. 1127, 1136-1139 (1979); 5C A. Jacobs, *Litigation and Practice Under Rule 10b-5* § 235.02 (rev. 2d ed. 1990). The two approaches frequently lead to divergent results. Compare *O'Hara* v. *Kovens*, 625 F.2d 15 (4th Cir. 1980) (using "commonality of purpose" approach and selecting state blue sky law period), cert. denied, 449 U.S. 1124 (1981), with *Wood* v. *Combustion Eng'g, Inc.*, 643 F.2d 339 (5th Cir. 1981) (applying "substantive resemblance" test and selecting state fraud period).

[4] See *O'Hara* v. *Kovens*, 625 F.2d at 18 (applying the one-year Maryland blue sky law limitations period, Md. Corp. & Ass'ns Code Ann. 11-703(f)); *Denny* v. *Performance Sys., Inc.* [1971-1972] Fed. Sec. L. Rep. (CCH) 93,387 (M.D. Tenn. 1971) (applying Tennessee's ten-year limitations period governing fraud, Tenn. Code Ann. § 28-310); see generally American Bar Association, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 646 (1985). See also Gov't Amicus Br. App. 1a-4a, *Lebman* v. *Aktiebolaget Electrolux*, No. 88-1114, cert. denied, 109 S. Ct. 3214 (1989). (We have provided the parties here with a copy of our brief in *Lebman*.)

[5] The first case of which we are aware to consider the applicable statute of limitations for Section 10(b) claims was *Osborne* v. *Mallory*, 86 F. Supp. 869 (S.D.N.Y. 1949). There, the court applied New York's six-year statute of limitations governing fraud. The first appellate court to consider the issue also chose the New York

follow that approach,[6] although more recently courts have gravitated toward borrowing the limitations periods governing blue sky private remedies.[7] Other courts of appeals, however, apply either the forum state's blue sky limitations period or the state's common law fraud period depending on the State within the circuit.[8] One court of appeals applies the period governing personal injury actions.[9]

The unpredictability fostered by inconsistent approaches to selecting the applicable period is exacerbated by the uncertainty surrounding subsidiary issues. Conflict-of-laws principles, as applied to securities transactions touching many States, make matters particularly unpredictable. Further uncertainty can result when the borrowed state law has been changed or amended. Confused and inconsistent approaches to questions such as tolling inject another level of uncertainty.[10] Deciding which features of state periods to adopt "wastes untold

six-year statute of limitations. *Fischman* v. *Raytheon Mfg. Co.*, 188 F.2d 783 (2d Cir. 1951).

[6] *Nesbit* v. *McNeil*, 896 F.2d 380 (9th Cir. 1990); *Bath* v. *Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817 (10th Cir. 1990).

[7] See *O'Hara* v. *Kovens*, *supra*; *Morris* v. *Stifel, Nicolaus & Co.*, 600 F.2d 139 (8th Cir. 1979); *Forrestal Village, Inc.* v. *Graham*, 551 F.2d 411 (D.C. Cir. 1977); see also *Friedlander* v. *Troutman, Sanders, Lockerman & Ashmore*, 788 F.2d 1500 (11th Cir. 1986).

[8] Compare *Herm* v. *Stafford*, 663 F.2d 669 (6th Cir. 1981) (applying Kentucky's three-year limitations period governing blue sky law claims), with *Gaudin* v. *KDI Corp.*, 576 F.2d 708 (6th Cir. 1978) (applying a four-year limitations period from Ohio's general fraud statute). Compare *Wood* v. *Combustion Eng'g, Inc.*, *supra* (applying a two-year limitations period governing claims under the Texas actionable fraud statute), with *Jensen* v. *Snellings*, 841 F.2d 600 (5th Cir. 1988) (applying Louisiana's two-year blue sky law period).

[9] *Maggio* v. *Gerard Freezer & Ice Co.*, 824 F.2d 123 (1st Cir. 1987).

[10] See Special Project, *Time Bars in Specialized Federal Common Law: Federal Rights of Action and State Statutes of Limitations*, 65 Cornell L. Rev. 1011, 1084-1095 (1980).

hours." *Norris* v. *Wirtz*, 818 F.2d 1329, 1332 (7th Cir.), cert. denied, 484 U.S. 943 (1987).

Recently, the Second, Third, and Seventh Circuits have charted a new course.[11] Those courts have held that the limitations periods governing certain of the express causes of action under the federal securities laws are the most appropriate source from which to draw a limitations period for Rule 10b-5 actions. We disagree with those courts that some variation of the one-year-from-discovery, but no-more-than-three-years-from-the-violation periods, provided more than a half century ago in the original securities acts, is the appropriate limitations period for Rule 10b-5 claims. We do believe, however, that a uniform federal limitations period should be applied to such private actions. In our view, the five-year limitations period in Section 20A of the Exchange Act, enacted in the Insider Trading and Securities Fraud Enforcement Act of 1988, Pub. L. No. 100-704, § 5, 102 Stat. 4681, affords Congress's most recent views on the accommodation of competing interests, provides the closest federal analogy, and promises to yield the best practical and policy results in Rule 10b-5 litigation.[12]

B. The Statute Of Limitations For A Federal Claim Having No Express Limitations Period May Be Drawn From Federal Law In Appropriate Cases

In a recent series of decisions, this Court has clarified the analytical framework for determining the appropriate statute of limitations when a federal statute is silent with respect to the applicable limitations period. "[A] clear majority of the Court [has] rejected [the] single path" of resorting only to state law, *Agency Holding Corp.* v. *Malley-Duff & Associates, Inc.*, 483 U.S.

[11] See *In re Data Access Systems Securities Litigation*, 843 F.2d 1537 (3d Cir.), cert. denied, 488 U.S. 849 (1988); *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990), petition for cert. pending, No. 90-526; *Ceres Partners* v. *GEL Associates*, No. 89-7666 (2d Cir. Nov. 8, 1990).

[12] Section 20A of the Exchange Act, 15 U.S.C. 78t-1, is reproduced in the appendix to this brief.

143, 146 (1987), and has ruled that the Court's task is to select "the most suitable statute or other rule of timeliness from * * * [a] source" in state or federal law. *DelCostello* v. *International Bhd. of Teamsters*, 462 U.S. 151, 158 (1983).[13]

The first step of the inquiry is to determine "whether all claims arising out of the federal statute 'should be characterized in the same way, or whether they should be evaluated differently depending upon the varying factual circumstances and legal theories presented in each individual case.'" *Agency Holding Corp.*, 483 U.S. at 147; *Reed* v. *United Transp. Union*, 488 U.S. 319, 325-326 (1989) (adopting uniform characterization where necessary to avoid "[t]ime-consuming litigation as to [a] collateral question" that would divert resources and discourage the assertion of claims under Section 101(a)(2) of the Labor Management Reporting and Disclosure Act, 29 U.S.C. 411(a)(2)).[14] The characterization of a federal claim for this purpose is usually governed by fed-

[13] This inquiry is not one into actual "legislative intent"; as this Court has recognized, in the usual case where Congress has failed to supply a limitations period, there is no indication of congressional intention on the issue at all. *DelCostello*, 462 U.S. at 158-159 n.12. Moreover, when an action is implied under a regulation, as is the case with Rule 10b-5, there is even less likelihood that Congress harbored an "intention" on a subsidiary procedural detail such as a limitations period. Thus, the issue does not turn on an inquiry into what statute of limitations the 73d Congress would have selected for Section 10(b); that Congress could not, in reason, have anticipated the current scope of Rule 10b-5. See *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 721, 737 (1975) (recognizing that the intent of the 73d Congress in 1934 does not afford insight into the proper construction of Rule 10b-5); cf. *Huddleston*, 459 U.S. at 385-386 (noting more recent congressional ratification of Rule 10b-5). See also Gov't Amicus Br. 9 n.14 in *Lebman* v. *Aktiebolaget Electrolux*, No. 88-1114, cert. denied, 109 S. Ct. 3214 (1989).

[14] See also *Wilson* v. *Garcia*, 471 U.S. 261 (1985) (selecting a uniform state personal injury analogy for all claims arising under 42 U.S.C. 1983); *Owens v. Okure*, 488 U.S. 235 (1989) (clarifying that the general or residual personal injury statute, rather than the intentional torts statute, should apply in actions under Section 1983).

eral law. *Agency Holding Corp.*, 483 U.S. at 147; *Wilson* v. *Garcia*, 471 U.S. 261, 269-270 (1985).

The second step is "whether a federal or state statute of limitations should be used." *Agency Holding Corp.*, 483 U.S. at 147. In view of the Court's historical borrowing of state law, it can generally be assumed "that Congress intends by its silence that we borrow state law." *Ibid.* However, " 'state statutes of limitations can be unsatisfactory vehicles for the enforcement of federal law,' " *ibid.*, quoting *DelCostello*, 462 U.S. at 161, in which event a federal statute may supply the better choice.

> [R]esort to state law remains the norm for borrowing of limitations periods. Nevertheless, when a rule from elsewhere in federal law clearly provides a closer analogy than available state statutes, and when the federal policies at stake and the practicalities of litigation make that rule a significantly more appropriate vehicle for interstitial lawmaking, we have not hesitated to turn from state law.

DelCostello, 462 U.S. at 171-172.

Four Terms ago, the Court applied that two-step analysis and held that the Clayton Act limitations period, 15 U.S.C. 15b, rather than state statutes of limitations, should govern civil RICO claims. *Agency Holding Corp.*, 483 U.S. at 148-157. See also *DelCostello*, *supra* (applying limitations period provided in Section 10(b) of the National Labor Relations Act to Section 301/fair representation claims); *Occidental Life Ins. Co.* v. *EEOC*, 432 U.S. 355 (1977) (refusing to apply a state statute of limitations to EEOC enforcement actions); *McAllister* v. *Magnolia Petroleum Co.*, 357 U.S. 221 (1958) (applying federal limitations period to unseaworthiness action under maritime law); *Holmberg* v. *Armbrecht*, *supra* (applying federal doctrine of laches, rather than state limitations period, to equitable enforcement of federal right). Here, the same principles mandate the adoption for Section 10(b) and Rule 10b-5 of the five-year limitations period found in Section 20A of the Exchange Act.

C. The Five-Year Statute of Limitations Drawn From Section 20A Should Govern All Rule 10b-5 Claims

1. *All private Rule 10b-5 claims should be characterized in a consistent way.* Applying the first step in the analysis, we believe that all Rule 10b-5 claims deserve a consistent characterization for selecting the appropriate statute of limitations. Like RICO and Section 1983, Section 10(b) and Rule 10b-5 "encompass numerous and diverse topics and subtopics." *Data Access*, 843 F.2d at 1543. An action under Section 10(b) and Rule 10b-5 "can be brought by a purchaser or seller of '*any* security' against '*any* person' who has used '*any* manipulative or deceptive device or contrivance'." *Huddleston*, 459 U.S. at 382. This sweeping language encompasses claims that, on their particular facts, may be analogized to actions for common law fraud, breach of fiduciary duty, breach of contract, misappropriation, and violations of blue sky laws, among others. See p. 24 n.36, *infra* (describing examples of Rule 10b-5 claims).

In view of the broad remedial purposes animating the federal securities laws, see, *e.g.*, *Huddleston*, 459 U.S. at 386-87, legal rules that serve the goal of "facilitating Rule 10b-5 litigation" promote the "congressional policy embodied in the 1934 Act." *Basic Inc.* v. *Levinson*, 485 U.S. at 245. Protracted disputes over the collateral issue of the appropriate statute of limitations disserve the legislative purpose of facilitating an effective remedy for defrauded investors. Under these circumstances, uniform characterization "is required to avoid intolerable 'uncertainty and time-consuming litigation.' " *Agency Holding*, 483 U.S. at 150, quoting *Wilson* v. *Garcia*, 471 U.S. at 272.

2. *No state law claim provides a suitable analogy for Rule 10b-5 claims.* For many of the same reasons, there is no adequate state law analogy for Rule 10b-5 claims. The inability of the lower courts to agree on an appropriate period, despite decades of litigation, highlights the shortcomings of state law. A comparison of the two leading contenders—common law fraud and blue sky law—serves to illustrate the problem.

Common law fraud actions initially appealed to courts seeking a Rule 10b-5 analogue. Yet, this Court has observed that common law fraud doctrines were developed in contexts "light years away from the world of commercial transactions to which Rule 10b-5 is applicable." *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723, 744-745 (1975). Indeed, one of Congress's paramount objectives in enacting Section 10(b) was to "rectify perceived deficiencies in the available common law protections by establishing higher standards of conduct." *Huddleston*, 459 U.S. at 389. Thus, "[a]ctions under Rule 10-b are distinct from common-law deceit and misrepresentation claims * * * and are in part designed to add to the protections provided investors by the common law." *Basic Inc.* v. *Levinson*, 485 U.S. at 244 n.22. In view of these differences, common law fraud provides only a rough analogy to claims under Section 10(b) and Rule 10b-5—and the limitations period governing common law fraud provides only a crude approximation of the balance of competing interests at stake in Section 10(b) private litigation.

Likewise, the blue sky civil remedy provisions generally vary in significant respects from claims under Section 10(b) and Rule 10b-5. Many jurisdictions have adopted antifraud provisions patterned after Section 410(a) of the Uniform Securities Act, which provides an express private right of action similar to Section 12(2) of the Securities Act of 1933 (Securities Act or 1933 Act), 15 U.S.C. 77*l*(2). Like Section 12(2), but unlike Section 10(b), these blue sky provisions do not require proof of scienter, reliance, or causation. Significantly, blue sky civil remedy provisions "come[] in a variety of shapes and sizes" varying considerably from state to state. L. Loss, *Fundamentals of Securities Regulation* 877-879 (2d ed. 1988). In view of the nuances and variation among the state securities laws, their limitations periods do not provide a promising source for a uniform, predictable rule.

3. *Section 20A of the Exchange Act provides a closer analogy to Rule 10b-5 than do state law alternatives.*

Here, as in *Agency Holding Corp.*, 483 U.S. at 150, "it is a *federal* statute that offers the closest analogy" to Rule 10b-5—Section 20A of the Exchange Act, 15 U.S.C. 78t-1. Indeed, Section 20A is more than a mere "analogy." It provides an express cause of action (on behalf of certain victims of insider trading) based on violations of the very provisions at issue here, Section 10(b) and Rule 10b-5. Section 20A codifies an express private right of action on behalf of persons trading contemporaneously in the market against "[a]ny person who violates any provision of this title or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information."[15] Section 20A(b)(4), 15 U.S.C. 78t-1(b)(4), sets forth an express statute of limitations:

> No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

Unlike any other express action in the federal securities laws, Section 20A specifically authorizes recovery for a particular type of Rule 10-5 violation. Actions brought under Section 20A, based on Rule 10b-5 violations, therefore require the plaintiff to establish the same elements of the violation as any claim brought under Rule 10b-5: (1) that the defendant engaged in fraud or manipulation, *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 471-474 (1977); (2) that he acted with scienter, *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185, 193 (1976); (3) that the misconduct related to a "material" fact, *Basic Inc.* v. *Levinson*, 485 U.S. at 238; and (4) that the misconduct occurred "in connection with" a securities transaction, *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. at

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[15] A principal purpose of this provision was "to overturn court cases which [had] precluded recovery for plaintiffs where the defendant's violation is premised upon the misappropriation theory [of insider trading]." H.R. Rep. No. 910, 100th Cong., 2d Sess. 26 (1988), citing *Moss* v. *Morgan Stanley*, 719 F.2d 5 (2d Cir. 1983), cert. denied, 465 U.S. 1025 (1984).

749.[16] Moreover, a claim under Section 20A, when premised on a violation of Rule 10b-5, is designed to further the same federal antifraud policies vindicated in any lawsuit under Section 10(b).[17]

Although Section 20A is addressed solely to insider trading, that consideration does not undermine its comparability to other Rule 10b-5 violations for purposes of choosing a limitations period. Contrary to the Second Circuit's view that Section 20A has "no relationship" to many types of Section 10(b) claims, *Ceres Partners* v. *GEL Associates*, No. 89-7666 (Nov. 8, 1990), slip op. 7271, the correspondence of elements required to establish a *violation* creates a compelling "analogy" between Section 20A and Rule 10b-5 generally; no other express cause of action under the securities laws reflects that match.[18] Moreover, the competing policies that Congress had to balance in enacting Section 20A's five-year limitations period, in the context of legislation dealing with insider trading, carry over to other forms of action based on Rule 10b-5. As the Second Circuit noted, a central

[16] Section 20A also imposes certain additional requirements (such as that the defendant and plaintiff have purchased or sold the same class of securities contemporaneously), but those differences from the requirements of other Rule 10b-5 actions are relatively minor.

[17] Congress enacted Section 20A knowing that insider trading violations involving Rule 10b-5 form a particular category of the general right of action under Rule 10b-5. See H.R. Rep. No. 910, 100th Cong., 2d Sess. 8 (1988).

[18] Nor does Congress's choice of a five-year period for Section 20A imply that other types of Rule 10b-5 claims should be subject to a different limitations period. In the statute itself, Congress signaled its intent that courts should continue to develop the incidents of the law governing the implied rights of action such as that recognized under Rule 10b-5. See 15 U.S.C. 78t-1(d). The legislative history, in discussing the substantive law, explained that Congress intended to "avoid * * * freezing the law or in any way restricting the potential rights of action which have been implied by the courts in this area," but instead to give "the courts leeway to develop such private rights of action in an expansive fashion in the future." H.R. Rep. No. 910, *supra*, at 27. See also 134 Cong. Rec. H7470 (daily ed. Sept. 13, 1988) (remarks of Rep. Lent); *id.* at S17,220 (daily ed. Oct. 21, 1988) (remarks of Sen. Garn).

concern of Congress was to address "the difficulties of ferreting out evidence sufficient to prosecute insider trading cases," *Ceres Partners*, slip op. 7271. Other Rule 10b-5 plaintiffs face equally daunting problems in ferreting out evidence of fraud.[19] Consequently, Congress's accommodation of policies, in determining to limit fraud claims under Section 20A by a five-year statute, fairly reflects the appropriate balance in other Rule 10b-5 contexts as well.[20]

4. *Policy and practical considerations favor Section 20A over state law.* There are compelling reasons to reject the application of state law to Rule 10b-5 claims. A principal purpose of the Exchange Act is to regulate the securities markets, which are inherently national in scope. See *Blue Chip Stamps*, 421 U.S. at 744-745. The securities laws are built around a jurisdictional nexus to interstate commerce or the mails, and were enacted in part because no single State's laws are capable of regulating the Nation's capital markets. See 15 U.S.C. 78b. Cf. *Agency Holding Corp.*, 483 U.S.C. at 153-154. "Congress enacted a national rule against fraud because it believed that national law ought to govern multistate transactions. Returning to state law to fetch a period of limitations is inconsistent in spirit with this decision." *Short* v. *Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1388

[19] For example, frauds based on "Ponzi" schemes can easily be concealed for several years—enough to ensure the running of a short statute of limitations for many claims. And "[a] similar situation often occurs in connection with defaulted municipal bond issues, an area of Rule 10b-5 securities fraud that may well involve more damages to investors on a national level than any other." Guin & Donaldson, *The Insider Trading and Securities Fraud Enforcement Act: Has Congress Supplied A Limitations Period Appropriate For Use In Private 10b-5 Actions?*, 47 Wash. & Lee L. Rev. 541, 569 (1990).

[20] Congress chose the same five-year limitations period for Commission penalty actions for insider trading violations. See 15 U.S.C. 78u-1(2) (authorizing penalty of up to three times profit gained or loss avoided), 78u-1(d)(5) (barring action "more than 5 years after the date of purchase or sale"). See H.R. Rep. No. 355, 98th Cong., 2d Sess. 12 (1984).

(7th Cir. 1990), petition for cert. pending, No. 90-526; see *Ceres Partners*, slip op. 7266.

Moreover, reference to state limitations periods under Rule 10b-5 results "in wholly unjustified disparities in the rights of parties litigating identical claims in different states." American Bar Association, *Report of the Task Force on Statute of Limitations for Implied Actions*, 41 Bus. Law. 645, 647 (1986) (hereinafter *ABA Report*). Multidistrict cases and class actions starkly illuminate those disparities.[21] Not only are different limitations periods unfair, they also invite use of the broad venue provisions of the securities laws to engage in forum shopping. *Ibid.* Although conflicts principles and borrowing statutes may discourage abuses, the application of choice-of-law doctrines complicates an already baffling and unpredictable process. Given the multistate nature of claims under Section 10(b) and Rule 10b-5, the borrowing of state law has resulted in "complex and expensive litigation over what should be a straightforward matter." *Agency Holding Corp.*, 483 U.S. at 154.

Courts[22] and commentators[23] agree that federal policy

[21] See, *e.g.*, *In re Clinton Oil Co. Securities Litigation*, [1977-1978] Fed. Sec. L. Rep. (CCH) ¶ 96,015 (D. Kan. 1977) (transferee court in multidistrict litigation was forced to select different limitations periods for each of several consolidated actions involving the identical violation). See also *Pinney* v. *Edward D. Jones & Co.*, 735 F. Supp. 915 (W.D. Ark. 1990) (discussing five options available to courts attempting to set limitations periods applicable to non-resident class claims); *Kronfeld* v. *Advest, Inc.*, 675 F. Supp. 1449, 1457-1458 & n.21 (S.D.N.Y. 1987) (borrowing statute resulted in application of at least 26 separate statutes of limitations).

[22] See *Data Access*, 843 F.2d at 1549 ("A broker in New York, an issuer in Delaware, a purchaser in San Francisco, an accountant in New Jersey, and a lawyer in Pennsylvania should be subject to the same statute of limitations for actions based on Section 10(b) or Rule 10b-5."); *Short*, 908 F.2d at 1389 ("From the perspective of practitioners litigating cases originating in many states * * *, the situation is a nightmare."); *Norris*, 818 F.2d at 1332 (describing approaches to subsidiary limitations issues created by reference to state law as a "tottering parapet of a ramshackle edifice").

[23] *ABA Report*, *supra*, at 656; L. Loss, *supra*, at 994-996; Ruder & Cross, *Limitations on Civil Liability Under Rule 10b-5*, 1972 Duke

and the efficiency of litigation are impaired by the borrowing of state law. The use of a limitations period drawn from Section 20A eliminates the quagmire that has resulted from looking to a "grab-bag," L. Loss, *supra*, at 995, of more or less analogous state statutes. It ensures that federal interests are protected by a defined, nationally uniform limitations period that is suited to the policies underlying the securities laws.

D. The One-And-Three-Year Limitations Periods Governing Certain Express Causes of Action In The Federal Securities Laws Should Not Be Applied To Rule 10b-5

The competing federal alternative to Section 20A is some form of the one-and-three-year limitations periods applicable to the express causes of action in the 1933 Act and to certain of the express actions in the 1934 Act. Congress, acting for the first time in 1988 to codify a private right based on a Section 10(b) violation, did not select those periods. Likewise, in our view, this Court should not apply those periods to Section 10(b) private actions generally.[24]

1. *The one-and-three-year periods apply to rights of action that are not more analogous to Rule 10b-5 than is Section 20A.*

a. Rule 10b-5 differs from the express rights of action that are subject to the one-and-three-year periods in the

L.J. 1125, 1142-1150; 2 T. Hazen, *The Law of Securities Regulation* § 13.8, at 127-128, 133 (2d ed. 1990); Schulman, *Statutes of Limitation in 10b-5 Actions: Complication Added to Confusion*, 13 Wayne L. Rev. 635 (1967); Block & Barton, *Statute of Limitations in Private Actions Under Section 10(b)—A Proposal for Achieving Uniformity*, 7 Sec. Reg. L.J. 374 (1980).

[24] *Data Access*, which initiated the move to a federal period, was decided before Congress enacted Section 20A. Both the Second Circuit in *Ceres* and the Seventh Circuit in *Short* chose a one-and-three-year format over Section 20A. But the Seventh Circuit acknowledged that "[c]hoosing between these statutes is difficult," *Short*, 908 F.2d at 1390, and one of the primary reasons supporting that court's decision—the desire to avoid creating a conflict with the Third Circuit (*id.* at 1390-1391)—does not apply to this Court, and indeed was not even accomplished by the Seventh Circuit's holding, see pp. 22-23, *infra*.

1933 and 1934 Acts in ways that substantially undercut the force of any analogy between those rights and Rule 10b-5.[25] Sections 11 and 12 of the 1933 Act, 15 U.S.C. 77k, 77*l*, unlike Section 10(b), provide remedies that do not require the plaintiff to prove scienter, reliance, or causation and that shift certain burdens of proof to the defendant. See L. Loss, *supra*, at 883-886, 887-895, 896-900.[26] Section 9 of the 1934 Act, 15 U.S.C. 78i—unlike

[25] The 1933 Act contains one-and-three-year statutes of limitations for the express rights of action brought under Sections 11 and 12 of the 1933 Act, 15 U.S.C. 77k, 77*l*. Section 11 creates a private right of action for false registration statements. Section 12(1) creates a private right of action predicated on the unlawful sale of unregistered securities. Section 12(2) creates a private right of action for the sale of securities through false or misleading statements. Section 13, 15 U.S.C. 77m, sets forth the applicable limitations periods.

The 1934 Act contains one-and-three-year statutes of limitations for the express rights of action created under Sections 9, 18, and 29. Section 9(e), 15 U.S.C. 78i, creates a private right of action for certain proscribed types of manipulation of security prices on national securities exchanges. Section 18(a), 15 U.S.C. 78r(a), creates a private right of action for misleading statements in applications, reports, or documents filed with the Commission. Section 29(b), 15 U.S.C. 78cc(b) (added by the Act of June 25, 1938, ch. 677, § 3, 52 Stat. 1076), permits rescission of certain purchases or sales of a security in violation of the Exchange Act or rules thereunder, and provides a one-and-three-year limitations period for private rescission actions based on violations of any regulation under 15 U.S.C. 78*o*(c)(1).

[26] As this Court has recognized, Section 11 is "limited in scope", "places a relatively minimal burden on a plaintiff," and "address[es] different types of wrongdoing" than Section 10(b). *Huddleston*, 459 U.S. at 382; see *ibid.* ("a § 10(b) plaintiff carries a heavier burden than a § 11 plaintiff"). Section 12(1) is virtually a strict liability provision for violation of the registration provision of the 1933 Act, 15 U.S.C. 77e. And, for the reasons noted in the text, the Seventh Circuit's observation in *Short* that Section 12(2) "describes the offense to which Rule 10b-5 is applied," 908 F.2d at 1390, is inaccurate. In fact, the Rule 10b-5 analogue in the 1933 Act is Section 17(a), 15 U.S.C. 77q(a), for which Congress provided no express private right of action.

the flexible Section 10(b)—is aimed at a static range of particular manipulative practices, and applies *only* to securities registered on a national securities exchange (and therefore has no application to the securities offered here).[27] Section 18 of the 1934 Act, 15 U.S.C. 78r, pertains only to false or misleading reports filed with the Commission (again, irrelevant here), and, unlike Section 10(b), does not require that the plaintiff prove scienter; in fact, it shifts the burden to the defendant to show good faith.[28] In contrast, private actions under Section 10(b) ordinarily require that the plaintiff prove scienter, reliance, and causation. Indeed, the 73d Congress enacted the relatively short limitations periods for the express rights in part because of the comparatively light burden placed on a plaintiff in an action under many of the express remedy provisions.[29]

[27] Although Section 9, like Section 10(b), requires proof of scienter and causation, Section 9, as this Court has recognized, focuses narrowly "upon the amount actually paid by an investor for stock that had been the subject of manipulative activity." *Piper* v. *Chris-Craft Indus., Inc.*, 430 U.S. 1, 46 (1977); see H.R. Rep. No. 1383, 73d Cong., 2d Sess. 11 (1934). Moreover, a shorter statute of limitations for that provision may be explained by its application exclusively to securities registered on a national securities exchange, which generally have wide distribution and are closely watched by the exchanges, investors, and the media. The owner of such securities may not need an extended period of time to discover the manipulation. In any event, as commentators have recognized, the private right under Section 9(e) "has been a dead letter so far as producing recoveries is concerned." L. Loss, *supra*, at 920.

[28] Section 18 has the "narrow and particularized objective of encouraging use of and reliance upon records" filed with the Commission, *Ross* v. *A.H. Robins Co.*, 607 F.2d 545, 556 (2d Cir. 1979), cert. denied, 446 U.S. 946 (1980), and therefore extends liability only to persons who make a misstatement in a report or other document filed with the Commission.

[29] As Senator Austin explained in the course of debate:

> I inquire of the Senator * * * whether he does not recognize another exceptional circumstance in that the burden of proof is shifted around on the question of knowledge or willfulness in a misrepresentation. The committee have put the burden on the defendant, so that in this case the plaintiff does not have to

This Court has shaped the private right of action under Section 10(b) with the understanding that the one-and-three-year limitations periods do not apply to it. In *Ernst & Ernst* v. *Hochfelder*, the Court held that scienter, rather than negligence, must be established in a Section 10(b) action. As one factor supporting that conclusion, the Court noted that while the express causes of action under the 1933 Act permit recovery on a negligence theory, they are subject to "significant procedural restrictions not applicable under § 10(b)," 425 U.S. at 208-209, including the one-and-three-year limitations period. *Id.* at 210. Section 10(b) claims, the Court observed, enjoyed the benefit of state statutes of limitations that "usually are longer than the period provided under [the 1933 Act]." *Id.* at 210 n.29. Because Section 10(b) claims lack the "procedural limitations" applicable to the express causes of action, the negligence standard of those provisions could not be extended to Section 10(b) "consistently with the intent of Congress." 425 U.S. at 210. Building on the same principle, *Herman & McLean* v. *Huddle-*

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spend any time going out and seeking his evidence. All he has to prove is the fact of misrepresentation.

78 Cong. Rec. 8201 (1934). Other statements made in the debate focus on the possibility that "technical" defects in a registration statement might create liability far into the future—a concern that is inapplicable to Rule 10b-5, which requires proof of intentional fraud and applies to much more than the initial offering of securities. See *id.* at 8199 (remarks of Sen. Kean) (expressing concern that persons might wait before suing over a "technical mistake in a [registration] statement"); *id.* at 8200 (remarks of Sen. Byrnes) (expressing concern that distant suits based on a misstatement in a registration statement might deter persons from serving on boards of directors). Some Senators focused on the desirability of requiring actions to be brought within a defined period after discovery of a violation. See *id.* at 8198 (remarks of Sen. Fletcher) ("[T]he thought was that a man ought not to delay suit more than 1 year after he discovers the fraud."). It is noteworthy that this one-year period, established in 1934 before Congress had gained experience with the operation of the securities laws, has not proved persuasive in the contemporary financial environment, as is evidenced by Congress's adoption in 1988 of a straightforward five-year provision in Section 20A.

ston concluded that the rights of action under Section 10(b) and Section 11 of the 1933 Act are cumulatively available to a defrauded investor. 459 U.S. at 381-387. In reaching that conclusion, the Court again relied on the differences between Section 11 and Section 10(b)—including the fact that while Section 10(b) requires scienter, it lacks procedural restrictions, such as a short statute of limitations. 459 U.S. at 384 n.18 (state limitations period for "§ 10(b) * * * is usually longer than the period provided for § 11 actions").

b. Quite apart from the fact that engrafting the one-and-three-year periods onto Section 10(b) is inconsistent with those aspects of *Hochfelder* and *Huddleston*, it is also crucial to note that there is no single "one-and-three-year" period in the securities laws; rather, there are only multiple variations on a theme, each uniquely fashioned for a particular express right of action. See L. Loss, *supra*, at 988-991.

Section 9(e) of the 1934 Act provides a period of one year after "discovery of the facts constituting the violation," but no more than three years after "such violation." 15 U.S.C. 78i(e). Section 18(c), in contrast, starts the one-year period after discovery of facts constituting "the cause of action," and bars suits three years after the cause of action "accrued." 15 U.S.C. 78r(c). And, Section 29(b)'s one-and-three-year periods are tied to the date of the "sale or purchase" involving the violation. 15 U.S.C. 78cc(b). These variations in language can produce strikingly different results when applied to the same set of facts.[30] Section 13 of the 1933 Act, in

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[30] The date of a Rule 10b-5 "violation" need not coincide with the "accrual" of a cause of action. In *Basic Inc.* v. *Levinson*, for example, the Rule 10b-5 violation was a company's issuance of false or misleading public statements denying it was engaged in merger talks. A class action was brought on behalf of shareholders who sold their stock in the company between October 1977 (the time of the first false statement) and December 1978 (when a merger was announced). 485 U.S. at 227-228. The "violation" occurred when false statements were made; the cause of action could not have "accrued" until each shareholder actually sold his stock. The results

turn, provides still other variations for each of its express rights of action. 15 U.S.C. 77m. In particular, claims under Sections 11 and 12(2)—unlike claims under Sections 9, 18, and 29 of the 1934 Act—must be filed within one year of actual or *constructive* discovery ("after such discovery should have been made by the exercise of reasonable diligence").[31] The three-year outside periods also begin to run from different events—after the security was "bona fide offered" for Section 11, but after the "sale" for Section 12(2).[32]

Although these variations can make a critical difference for the timeliness of any particular action, the courts of appeals that have embraced the one-and-three-year periods appear not to have appreciated the quandary. The Third Circuit, leading the way in *Data Access*, purported to apply the general one-and-three-year "schema" in the Exchange Act, 843 F.2d at 1546, but ultimately adopted a limitations period of "one year after the plaintiff discovers the facts constituting the violation, and in no event more than three years after such violation", *id.* at 1550, a formulation that corresponds to Section 9(e) of the 1934 Act.[33] The Seventh Circuit,

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of applying the limitations periods of Sections 9(e) and 18(c) would therefore diverge. In contrast, Section 20A(b)(4)'s test ("date of the last transaction that is the subject of the violation") would provide far greater certainty and ease of application.

[31] A Section 12(1) claim must be brought within one year "after the violation upon which it is based," but no more than three years "after the security was bona fide offered to the public".

[32] The 1933 Act limitations periods were originally two years and ten years, Act of May 27, 1933, ch. 38, § 13, 48 Stat. 84, but Congress shortened those periods when it amended the Securities Act in 1934. 48 Stat. 908. See *Ernst & Ernst* v. *Hochfelder*, 425 U.S. at 210.

[33] The court did not explain why it chose the Section 9 formulation. If the theory behind borrowing the one-and-three-year periods is that Section 10(b) and Rule 10b-5 are analogous to the *cumulative* scope of Sections 9, 18, and 29 of the 1934 Act, and Sections 11 and 12 of the 1933 Act, it is inconsistent with that rationale to conclude that the Section 9 limitations period in particular should be applied to *all* Section 10(b) claims.

following on the heels of *Data Access*, mistakenly thought that the Third Circuit had selected Section 13 of the 1933 Act; it then concluded that Section 12(2) formed the appropriate model for Rule 10b-5, and ultimately adopted Section 12(2)'s one-and-three-year limitations provision. *Short*, 908 F.2d at 1390-1391. But that provision includes a *constructive* discovery limitation on the one-year period, in conflict with the choice made by *Data Access*.[34] Finally, the Second Circuit held that Rule 10b-5 claims would be governed by "the statute of limitations provided in the 1934 Act for express rights of action under §§ 9(e) and 18(a) of that Act," *Ceres Partners*, slip op. 7274, even though the language of those two provisions differs. The three-way conflict generated by the courts of appeals underscores the futility of searching for an apt analogy in any of the express rights of action enacted in 1933 and 1934 for purposes of selecting the appropriate statute of limitations for Rule 10b-5.

2. *Policy considerations militate against the one-and-three-year system.* Applying the relatively short one-and-three-year periods frustrates important policy goals as well.[35] As the law has developed, Rule 10b-5 is vastly more important in combatting fraud than are the express remedies provided in the 1933 and 1934 Acts. Borrowing the shorter limitations periods found in those Acts for Rule 10b-5 would impede enforcement of the Rule's requirements, and would thereby impair the securities laws' function of protecting investors.

Section 10(b) and Rule 10b-5 have come to embrace a diversity of claims which could not have been envisioned in 1934. This Court has consistently construed those provisions broadly, noting that they "are obviously

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[34] In the Third Circuit, the one-year period is not subject to a constructive discovery limitation. See *Gruber* v. *Price Waterhouse*, 911 F.2d 960, 964 n.4 (1990).

[35] The Court has noted that policy considerations are relevant in delineating the contours of Rule 10b-5. See *Blue Chip Stamps*, 421 U.S. at 737, 749.

meant to be inclusive." *Affiliated Ute Citizens* v. *United States*, 406 U.S. 128, 151 (1972). See *Huddleston*, 459 U.S. at 386; *United States* v. *Naftalin*, 441 U.S. 768, 773 (1979).[36] By contrast, the express remedies governed by the one-and-three-year limitations periods are much more limited in scope. Indeed, the implication of a right of action under Rule 10b-5 is justified in part because the specific liabilities created by the express causes of action in the Exchange Act "do not cover all the variegated activities with which that act is concerned." 3 L. Loss, *Securities Regulation* 1785 (2d ed. 1961).

The one-and-three-year periods, if applied to Rule 10b-5, would deprive many defrauded investors of a satisfactory opportunity to vindicate their rights. Especially in complex cases, plaintiffs often "do not discover the fraud until long after its perpetration." *ABA Report*, *supra*, at 656.[37] Violations involving financial fraud, for instance, often go undetected until the enterprise fails, an event that may occur years after the violation. Moreover, as the securities markets have grown in size and complexity, frauds have become increasingly difficult to discover.[38] Thus, we do not agree with the

[36] Section 10(b) actions can be brought against the issuer of securities for false or misleading material public statements, see *Basic Inc.* v. *Levinson*, *supra*; against accountants, lawyers, or others involved in an offering of securities, see *Huddleston*, 459 U.S. at 378; against broker-dealers by customers fraudulently induced to purchase securities, see *Bateman Eichler, Hill Richards, Inc.* v. *Berner*, 472 U.S. 299, 301-303 (1985); against persons who trade in the securities market while in possession of non-public information in breach of a duty, cf. *Dirks* v. *SEC*, 463 U.S. 646, 653-654 (1983); against persons who manipulate the market for securities, cf. *Santa Fe Indus., Inc.* v. *Green*, 430 U.S. 462, 476-477 (1977); and in many other situations.

[37] Indeed, even the SEC with all its investigative resources and statutory powers, including compulsory investigative processes, does not complete its investigations, on average, in less than 2.25 years.

[38] Congress recognized these developments in recent amendments to the securities laws that provide the Commission additional enforcement remedies. See The Securities Enforcement Remedies and Penny Stock Reform Act of 1990, Pub. L. No. 101-429, 104 Stat.

Seventh Circuit's sanguine view that "[p]rudent investors can almost always sniff out fraud (or enough smoke to justify litigation) within three years," *Short*, 908 F.2d at 1392; in the Commission's experience, a considerable number of frauds are simply not detected within that period of time.

Because "the interests of plaintiffs in [Rule 10b-5] suits are significant," *Huddleston*, 459 U.S. at 390, and private actions "constitute[] an essential tool for enforcement of the 1934 Act's requirements", *Basic Inc.*, 485 U.S. at 231, the adequacy of a limitations period to serve the purposes of the Rule is an important consideration. In this case, application of the short one-and-three-year periods threatens to undermine the effectiveness of the Rule 10b-5 remedy. Cf. *Agency Holding Corp.*, 483 U.S. at 154 (rejecting use of "unduly short state statutes of limitations that would thwart the legislative purpose of creating an effective remedy"); *DelCostello*, 462 U.S. at 166, 167-168 (rejecting state limitations periods that were too short to vindicate federal rights).

3. *Applying the one-and-three-year periods would perpetuate uncertainty over limitations issues.* Adoption of a one-and-three-year provision would mean that actions based on Rule 10b-5 violations would be subject to two different statutes of limitations—those periods and Section 20A(b)(4). This would inevitably engender confusion. As the Seventh Circuit noted, "[c]lever lawyers could describe even a garden variety fraud as 'purchasing or selling a security while in possession of material, nonpublic information'—that is, the truth—blurring the line between the offenses and making the choice of a period of limitations difficult." *Short*, 908 F.2d at 1391.[39] Appli-

931; S. Rep. No. 337, 101st Cong., 2d Sess. 6 (1990) ("As the markets * * * have grown dramatically in size and complexity, particularly in the last decade, the SEC's law enforcement task has become increasingly difficult. Investigations involve more complex issues of fact and law."); 136 Cong. Rec. S10,011 (daily ed. July 18, 1990) (remarks of Sen. Dodd).

[39] The Seventh Circuit erroneously downplayed that confusion, however, because it incorrectly assumed (908 F.2d at 1391) that

cation of different periods to different types of claims based on Section 10(b) will give parties an incentive to engage in "artful pleading" in the hope of "persuad[ing] the court that the facts and legal theories of a particular * * * claim" fall within Section 20A's longer limitations period. *Owens* v. *Okure*, 488 U.S. 235, 240 (1989). Courts and parties would be called upon to wrestle with these characterization questions—a result which runs counter to the reasons for choosing a uniform federal rule in the first place. Section 20A eliminates those problems.

The problem with selecting the one-and-three-year periods is accentuated in Rule 10b-5 insider trading cases. In Section 20A, Congress codified a Rule 10b-5 cause of action for contemporaneous traders; the legislative history, however, acknowledged that "there clearly are injuries caused by insider trading to others beyond contemporaneous traders." H.R. Rep. No. 910, *supra*, at 27. For example, the Committee Report cited *Anheuser-Busch Co.* v. *Thayer*, No. CA3-0794-R (N.D. Tex. 1986), in

only an individual "insider," not the issuer itself, can be liable under Section 20A (in fact, both can be liable), and because it noted that persons suing under Section 20A "must accept the limitations of that statute, including the restriction of damages to the defendants' profit (as opposed to the plaintiff's loss)." *Ibid.* To a plaintiff who misses the three-year deadline, however, it is Section 20A or nothing; hence, the availability of damages, notwithstanding the measure, will provide ample incentive to sue. Moreover, the court of appeals was incorrect in believing that damages under Section 20A are unique in being fixed soon after the violation (908 F.2d at 1392); that is ordinarily the case in an action under Rule 10b-5 where the general measure of damages is "out-of-pocket" loss. See *Randall* v. *Loftsgaarden*, 478 U.S. 647, 661-662 (1986) (noting that damages are ordinarily "the difference between the fair value of all that the [plaintiff] received and the fair value of what he would have received had there been no fraudulent conduct"; leaving open the question whether rescissionary recovery may be appropriate in some cases). An out-of-pocket measure of damages does not allow the plaintiff, by "delay[ing] in bringing suit[,] to speculate on the firm's future prosperity," 908 F.2d at 1392. Where rescission is permitted, that measure fulfills a necessary role in deterring intentional fraud. Cf. *Randall*, 478 U.S. at 659; *Pinter* v. *Dahl*, 486 U.S. at 637 n.13 (discussing Section 12(2) of the 1933 Act).

which Anheuser-Busch sued one of its directors alleging that he had disclosed information about Anheuser-Busch's proposed acquisition of another firm to persons who purchased stock in the target company and thereby drove up the acquisition price. H.R. Rep. No. 910, *supra*, at 28. Although Congress did not cover that form of injury in Section 20A, the theory of *Anheuser-Busch* was recognized as a valid basis for recovery under Section 10(b). *Ibid.* As a result, when a defendant misappropriates information from an acquiring company, contemporaneous traders have five years to sue under Section 20A. But, if the one-and-three-year periods apply to other Rule 10b-5 actions, the acquiring firm—a direct victim of the fraud—would have a significantly shorter time to sue for the same violation. Anomalies like that serve no useful purpose and underscore the need for a single, consistent statute.

4. *Section 20A better reflects Congress's current appraisal of the relevant policies.* As a result of the passage of time and "the peculiar blend of legislative, administrative, and judicial history which now surrounds [the] Rule," *Blue Chip Stamps*, 421 U.S. at 749, the force of arguments for choosing the half-century old limitations periods in the 1933 and 1934 Acts for Rule 10b-5 has significantly diminished. For over 40 years, courts assumed that state limitations periods, and not the federal one-and-three-year periods, governed claims under Rule 10b-5. Since the one-and-three-year periods "are shorter than the typical periods in whatever state statutes the courts have looked to traditionally,"[40] applying them would represent a substantial retrenchment from the present state of the law.[41] In contrast, the five-year lim-

[40] L. Loss, *Fundamentals of Securities Regulation* 218 (2d ed. Supp. 1990). The Second Circuit's impression to the contrary in *Ceres Partners*, slip op. 7272, overlooked the fact that borrowed state periods are subject to federal equitable tolling.

[41] That factor may have influenced the American Law Institute's proposed *Federal Securities Code* § 1727(b) (1980), which would have provided a statute of limitations of one year from constructive

itations provision in Section 20A would better approximate the traditional state law periods, while providing the requisite uniformity.

The Seventh Circuit supported its preference for a one-and-three-year provision in part because of its belief that that period alone could secure an outer limit of "repose"; Section 20A, the court thought, may be subject to equitable tolling. *Short*, 908 F.2d at 1391-1392. We agree that the fixing of a defined point of repose is an important structural component of Congress's plan for private securities law actions. But the same benefit is available under Section 20A.

First, although the Court has stated that equitable tolling is "read into every federal statute of limitations," *Holmberg* v. *Armbrecht*, 327 U.S. at 397, the Court, to our knowledge, has never had occasion to apply that principle to a right of action *implied* from a statute containing *express* rights systematically governed by non-tollable limitations periods.[42] That is the situation with respect to Section 20A.

Second, the outside period of repose in the 1933 and 1934 Act periods reflects a general congressional policy against tolling of securities claims that applies equally

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discovery and five years from the violation for violations of the antifraud provision. The ABA Task Force proposed "a compromise of two years from the date of discovery, with a four-year cutoff." *ABA Report*, *supra*, at 658.

[42] The three-year period is not subject to equitable tolling. See, *e.g.*, *Data Access*, 843 F.2d at 1550; *Norris* v. *Wirtz*, 818 F.2d at 1332; *Zola* v. *Gordon*, 685 F. Supp. 354, 361 (S.D.N.Y. 1988) (citing cases). A unique limitations principle applies to Section 16(b) (two-year statute of limitations governing claims for recovery of profits realized by certain insiders in transactions involving a purchase and sale, or sale and purchase, within less than six months). 15 U.S.C. 78p(b). Those claims are subject to a quite distinct form of tolling flowing from the related requirement in Section 16(a) that an insider must report his securities transactions to the Commission. See *Whittaker* v. *Whittaker Corp.*, 639 F.2d 516, 528 (9th Cir.) (two-year period is tolled until the insider has filed a required report disclosing his transactions), cert. denied, 454 U.S. 1031 (1981).

to Section 20A. This policy stems from the view that, if tolling is available, potential defendants will be subject to contingent liabilities for indefinite periods.[43] Not only might this "deter [individuals] from serving on boards of directors" because of fear of lingering liabilities, 78 Cong. Rec. 8200 (1934) (remarks of Sen. Byrnes), it could make it more difficult for public companies to "assess the impact of possible litigation under rule 10b-5" for financial statement purposes, thereby possibly adversely affecting the accuracy of their disclosure and "depriv[ing] investors of information adequate for informed evaluation of such companies' potential liabilities" for a longer period of time. *ABA Report*, *supra*, at 646-47.

Third, the language of Section 20A(b)(4) suggests that tolling is inappropriate. In contrast to statutes in which the limitations period runs from the time the "cause of action accrued," [44] Section 20A(b)(4) provides a limitations period that runs from the "date of the last transaction that is the subject of the violation." [45] That is a much more exact starting point, especially since

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[43] See 78 Cong. Rec. 8198-8203 (1934); see also *ABA Report*, *supra*, at 655 (finding it "inescapable * * * that Congress did not intend equitable tolling to apply in actions under the securities laws"); Bloomenthal, *The Statute of Limitations and Rule 10b-5 Claims: A Study in Judicial Lassitude*, 60 U. Colo. L. Rev. 235, 257-264, 287-289 (1989) (same).

[44] See, *e.g.*, *Bailey* v. *Glover*, 88 U.S. (21 Wall.) 342, 344 (1874) (equitable tolling of bankruptcy claim).

[45] In the rare instance in which Congress has used language indicating a similarly exact starting point, one court has found the limitations period not subject to tolling. See *Hill* v. *Texaco*, 825 F.2d 333, 334-335 (11th Cir. 1987). We recognize that this Court recently rejected a rule that would have made the availability of equitable tolling against the government turn on the particular "phraseology" of a statutory time limit. *Irwin* v. *Veterans Administration*, No. 89-5867 (Dec. 3, 1990), slip op. 5. But this case is distinguishable, because even if Section 20(A)(b)(4)'s language, standing alone, were not sufficient, it certainly points to the rejection of tolling and the surrounding legislative scheme makes that the most plausible reading of the statute.

courts often view a cause of action as accruing at the date of discovery.[46]

Fourth, barring private actions after five years does not insulate the wrongdoer from all exposure; Rule 10b-5 actions brought by the Commission (except for certain penalty claims) are not subject to any limitations period.

In sum, a five-year non-tollable limitations period drawn from Section 20A would provide a more appropriate statute of limitations than the unduly short one-and-three-year periods, and would be in keeping with the important congressional interest in repose. Against that background, we see no adequate textual, historical, or policy justification for this Court to prefer a limitations period enacted by Congress more than half a century ago, with certain quite different and delimited rights of action in mind, over a limitations period that Congress so recently enacted for certain violations of Rule 10b-5 itself.[47]

CONCLUSION

A five-year limitations period drawn from Section 20A of the Securities Exchange Act, not subject to tolling, should be applied to claims under Section 10(b) and Rule 10b-5.

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[46] See, e.g., *United States* v. *Lovknit Mfg. Co.*, 189 F.2d 454, 457 (5th Cir.) ("Actions for fraud do not ordinarily accrue till the fraud is discovered or should with diligence have been discovered."), cert. denied, 342 U.S. 896 (1951).

[47] If the Court agrees with our view, the case should be remanded to the court of appeals for application of Section 20A(b)(4). Although it appears that most of respondents' claims would be time-barred, the ultimate conclusion is not clear. The complaints (but for respondent Catalan's) were filed on November 3, 1986, alleging fraud in connection with limited partnerships formed in 1979, 1980, and 1981. Claims relating to transactions prior to November 3, 1981, would be time-barred. However, to the extent that installment payments were made after that date (see Resp. C.A. Joint Br. 7), certain claims may survive under the "investment decision" doctrine (an issue on which we take no position). Cf. Note, *Defenses to the Statute of Limitations In Federal Securities Cases: The Fraudulent Concealment Doctrine and the Investment Decision Doctrine*, 38 S. C. L. Rev. 789, 815 (1987).

In addition, the retroactive application of shorter statutes of limitations raises questions under *Chevron Oil Co.* v. *Huson*, 404 U.S. 97, 106-107 (1971). Although Section 20A does not by its terms apply retroactively, see 102 Stat. 4684 (set forth at 15 U.S.C. 78o note), the question whether Section 20A(b)(4) should apply retroactively when *borrowed* for Rule 10b-5 actions is a matter for the courts to determine. Cf. *DelCostello*, 462 U.S. at 169-170 n.21. The court of appeals should initially determine whether such application is warranted here. Cf. *Short*, 908 F.2d at 1389-1390 (citing cases).

Respectfully submitted.

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APPENDIX

15 U.S.C. 78t-1 provides:

Liability to contemporaneous traders for insider trading

(a) Private rights of action based on contemporaneous trading

Any person who violates any provision of this chapter or the rules or regulations thereunder by purchasing or selling a security while in possession of material, nonpublic information shall be liable in an action in any court of competent jurisdiction to any person who, contemporaneously with the purchase or sale of securities that is the subject of such violation, has purchased (where such violation is based on a sale of securities) or sold (where such violation is based on a purchase of securities) securities of the same class.

(b) Limitations on liability

(1) Contemporaneous trading actions limited to profit gained or loss avoided

The total amount of damages imposed under subsection (a) of this section shall not exceed the profit gained or loss avoided in the transaction or transactions that are the subject of the violation.

(2) Offsetting disgorgements against liability

The total amount of damages imposed against any person under subsection (a) of this section shall be diminished by the amounts, if any, that such person may be required to disgorge, pursuant to a court order obtained at the instance of the Commission, in a proceeding brought under section 78u(d) of this title relating to the same transaction or transactions.

(3) Controlling person liability

No person shall be liable under this section solely by reason of employing another person who is liable under this section, but the liability of a controlling person under

this section shall be subject to section 78t(a) of this title.

(4) Statute of limitations

No action may be brought under this section more than 5 years after the date of the last transaction that is the subject of the violation.

(c) Joint and several liability for communicating

Any person who violates any provision of this chapter or the rules or regulations thereunder by communicating material, nonpublic information shall be jointly and severally liable under subsection (a) of this section with, and to the same extent as, any person or persons liable under subsection (a) of this section to whom the communication was directed.

(d) Authority not to restrict other express or implied rights of action.

Nothing in this section shall be construed to limit or condition the right of any person to bring an action to enforce a requirement of this chapter or the availability of any cause of action implied from a provision of this chapter.

(e) Provisions not to affect public prosecutions

This section shall not be construed to bar or limit in any manner any action by the Commission or the Attorney General under any other provision of this chapter, nor shall it bar or limit in any manner any action to recover penalties, or to seek any other order regarding penalties.

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No. 90-933

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETRIGROW,

Petitioner,

v.

JOHN GILBERTSON, ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF AND BRIEF OF THE NATIONAL ASSOCIATION OF SECURITIES AND COMMERCIAL LAW ATTORNEYS AS AMICUS CURIAE IN SUPPORT OF RESPONDENTS

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MOTION FOR LEAVE TO FILE BRIEF AS AMICUS CURIAE

Pursuant to Rule 37.3 of the Rules of this Court, the National Association of Securities and Commercial Law Attorneys ("NASCAT") respectfully moves for leave to file the enclosed brief as amicus curiae in support of respondents. Counsel for respondents has granted consent to file this brief. Counsel for petitioner also has granted consent to file this brief.

NASCAT is an association of law firms consisting of approximately 500 attorneys located throughout the United States whose purpose is to promote the enactment and enforcement of legislation which protects investors from deceptive and manipulative practices and ensures that the securities markets in the United States can operate in a fair and free manner. NASCAT members have represented plaintiffs in a variety of individual and class action contexts under

the federal securities laws; some NASCAT members have also represented defendants in securities and other cases.

NASCAT and its members have a strong interest in the effective private enforcement of the federal securities laws and in the development of case law that effectively deters would-be wrongdoers from perpetrating securities fraud upon public investors. Because of this Court's repeated endorsement of the flexible interpretation and need for private enforcement of the federal securities laws, the issues raised by this appeal are extremely important to the investment community and the capital markets generally.

The enclosed amicus curiae brief addresses selection of a statute of limitations to be applied to the right of action implied under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §240.10b-5.

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90-933

IN THE

Supreme Court of the United States

OCTOBER TERM, 1990

LAMPF PLEVA LIPKIND PRUPIS & PETIGROW,

Petitioner,

v.

JOHN GILBERTSON, ET AL.,

Respondents.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OF THE NATIONAL ASSOCIATION OF SECURITIES AND COMMERCIAL LAW ATTORNEYS AS AMICUS CURIAE IN SUPPORT OF RESPONDENTS

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QUESTION PRESENTED

Whether a non-tollable, one-year/three-year statute of limitations is appropriate for application to implied private actions under the antifraud provisions of Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §240.10b-5.

INTEREST OF THE AMICUS CURIAE

As explained in the foregoing motion for leave to participate as amicus curiae, NASCAT is a national association of law firms consisting of approximately 500 attorneys located throughout the United States whose purpose is to facilitate protection of investors and other consumers through appropriate legislative and judicial activity.

This Court has repeatedly emphasized the need for private enforcement of the federal securities laws, and has consistently recognized that the securities laws should be flexibly construed to achieve the remedial purposes of those laws. The limitations period which is applied to claims under Section 10(b) of the Securities Exchange Act of 1934 will have a direct effect on the enforcement of those laws. As such, the issues presented in this case are extremely important to the investment community and the capital markets generally.

SUMMARY OF THE ARGUMENT

The non-tollable one-year/three-year statute of limitations which petitioner proposes be applied to Section 10(b) claims is not drawn from the law "most analogous" to Section 10(b). Because the implied right of action under Section 10(b) is a fraud claim, the "most analogous" law is state common law fraud. If this Court decides to look to federal law, Section 20A of the Securities Exchange Act of 1934 is more "analogous" to Section 10(b) than the law from which the non-tollable, one-year/three-year statute of limitations is drawn. Moreover, the long-standing doctrine of equitable tolling must be applied to the limitations period selected for Section 10(b) claims. Finally, if this Court determines that a different limitations period should apply to Section 10(b) claims than the current use of state statutes of limitations applicable to analogous state law, that decision should not be retroactive.

I. A NON-TOLLABLE ONE YEAR/THREE YEAR STATUTE OF LIMITATIONS IS NOT APPROPRIATE FOR APPLICATION TO 10b-5 CLAIMS

The question presented in this case is straightforward: whether a judicially-created, non-tollable statute of limitations should govern the timeliness of the assertion of the implied private right of action under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. §78j(b), and Rule 10b-5 thereunder, 17 C.F.R. §240.10b-5 ("10(b)" or "10b-5")? Petitioner argues for a non-tollable one-year/three-year period of repose, relying on the Third Circuit's creation of such a period from limitation statutes contained in various sections of the Securities Act of 1933, 15 U.S.C. §77a *et seq.* (the "1933 Act") and the Securities Exchange Act of 1934, 15 U.S.C §78a, *et seq.* (the "1934 Act"). *In re Data Access Securities Litigation*, 843 F.2d 1537 (3d Cir.), *cert. denied*, 488 U.S. 849 (1988).[1]

After *Data Access*, the Seventh Circuit adopted a different non-tollable, one-year/three-year statute of limitations for application to Section 10(b) claims in *Short v. Belleville Shoe*

[1] In *Data Access*, the Third Circuit created a limitations period which runs one-year from constructive discovery of the violation, but in no event more than three years from the violation. *Id.* at 1550. This is a limitations period with no counterpart in either the 1933 or 1934 Acts. Guin and Donaldson, *The Insider Trading and Securities Fraud Enforcement Act: Has Congress Supplied A Limitations Period For Use In Private 10b-5 Actions?*, 47 Wash. & Lee L. Rev. 541, 563-65 (1990). *See also* Section I.B., *infra*.

Mfg. Co., 908 F.2d 1385 (7th Cir. 1990).[2] Most recently, the Second Circuit concluded that a third version of the one-year/three-year rule applied to Section 10(b) claims in *Ceres Partners v. GEL Associates*, 918 F.2d 349 (2d Cir. 1990).[3]

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[2] In *Short*, the Seventh Circuit incorrectly stated that "*Data Access* selected §13 [of the Securities Act of 1933] as the appropriate federal law. . . . " *Id.* at 1390. Yet, in *Data Access*, the Third Circuit clearly decided that "the express limitations sections of the Securities Exchange Act of 1934 provide the preferable source of limitations borrowing here." 843 F.2d 1550. The Third Circuit then created its own version of the one-year/three-year rule. *See supra* note 1. Section 13 of the 1933 Act provides:

> No action shall be maintained to enforce any liability under section 11 or section 12(2) unless brought within one year after the discovery of the untrue statement or the omission, or after such discovery should have been made by the exercise of reasonable diligence, or, if the action is to enforce a liability created under section 12(1), unless brought within one year after the violation upon which it is based. In no event shall any such action be brought to enforce a liability created under section 11 or section 12(1) more than three years after the security was bona fide offered to the public, or under section 12(2) more than three years after the sale.

15 U.S.C. §77(m). The Seventh Circuit in *Short*, held that Section 13 governed Rule 10b-5 claims and applied Section 13 to determine that plaintiff's claim was untimely filed. 908 F.2d at 1392-93.

[3] In *Ceres*, the Second Circuit incorrectly observed that the Seventh Circuit in *Short* concluded that "a more appropriate analogy than state limitation statutes was to be found in the 1934 Act itself." *Id.* at 359. In fact, in *Short*, the Seventh Circuit adopted Section 13 of the 1933 Act as the limitations period for Section 10(b) claims. *See supra* note 2. The Second Circuit in *Ceres*, concluded "that the statute of limitations provided in 1934 Act for express rights of action under §9(e) and 18(a)" should apply to Section 10(b) claims. *Ceres*, 981 F.2d 364.

Section 9(e) of the 1934 Act provides:

> No action shall be maintained to enforce any liability created under this section, unless brought within one year after the discovery of the facts constituting the violation and within three years after such violation.

15 U.S.C. §78i(e). Section 18(c) of the 1934 Act states:

(footnote continues)

While non-tollable statutes of repose may be appropriate for the express rights of actions contained in the 1933 and 1934 Acts, any of the three limitation periods now being applied in the Third, Seventh and Second Circuits will hinder and in many cases eliminate the private enforcement of the federal securities laws now provided by 10b-5 actions. Moreover, the one-year/three-year rule stands in sharp contrast to this Court's mandate that the federal securities laws "should be construed 'not technically and restrictively, but flexibly to effectuate [their] remedial purposes.'" *Herman & MacLean v. Huddleston*, 459 U.S. 375, 386-87 (1983) (citations omitted).

The one-year/three-year rule will certainly reduce 10b-5 litigation, but at an unacceptable cost. Defrauded investors, who have relied upon the integrity of this country's capital markets, will be left without recourse or remedy under the very federal laws that were designed to protect them, while the perpetrators of fraud will not be held to account for their conduct. Such a result is inconsistent with (i) a flexible construction of the securities laws designed to achieve the remedial purposes of those laws; and (ii) other federal procedural requirements, including Rules 9(b) and 11 of the Federal

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(footnote continued)

> No action shall be maintained to enforce any liability created under this section unless brought within one year after the discovery of the facts constituting the cause of action and within three years after such cause of action accrued.

15 U.S.C. §78r(c).

Thus, plaintiffs and defendants in the Second Circuit are faced with the question whether the three year period commences with the "violation" or accrual of the "cause of action."

Rules of Civil Procedure, which were adopted to discourage overly precipitous fraud actions.[4]

The Supreme Court has outlined the following process for selecting a statute of limitations to be applied to a cause of action when Congress is silent on the questions (*Agency Holding Corp. v. Malley-Duff & Assoc., Inc.*, 483 U.S. 143, 147 (1987)):

> 1. The first step in selecting the appropriate statute of limitations is to characterize the federal claim (which is usually a question of federal law), by determining whether all claims arising out of the federal statute will be characterized in the same way, or evaluated differently depending upon the facts and legal theories of each claim. *Id.*
>
> 2. The next question is whether a federal or state statute of limitations should be applied. The Rules of Decision Act, 28 U.S.C. §1652, requires the use of a state statute; only in limited circumstances (483 U.S. at 147) should a limitations statute "from elsewhere in the federal law . . . be applied." *DelCostello v. International Bhd. of Teamsters*, 462 U.S. 151, 159 n. 13.

[4] Judge Easterbrook's comments in the Seventh Circuit's *Short* opinion demonstrate an insensitivity both to the plight of a defrauded investor caught between the *Short* limitations period and Rules 9(b) and 11, and to this Court's long history of support for a flexible construction of the securities laws. In *Short*, Judge Easterbrook noted that with a shorter period of time, investors will "have a more powerful incentive to investigate rather than accept another person's word without question. . . . Prudent investors can almost always sniff out fraud (or enough smoke to justify litigation) within three years. *Section 13 cuts off only the claims of the most trusting* or somnolent — or the most wily, those who wanted to wait as long as possible." *Short*, 908 F.2d at 1392 (emphasis added). Fortunately, investors can look to this Court's firm and unwavering support of the protections afforded by the federal securities laws.

> 3. A statute of limitations from elsewhere in the federal law may be appropriate if the characterization of the federal claim leads to the conclusion that state statutes of limitation are "unsatisfactory vehicles for the enforcement of federal law." *Id.* at 161.
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> 4. The court must then determine that (i) there is a rule in federal law which provides a closer analogy than available state statutes, and (ii) federal policies at stake and the practicalities of litigation make the federal rule "a significantly more appropriate vehicle for interstitial lawmaking. . . . " *Id.* at 171-72.

Agency Holding, 483 U.S. at 147-48.

A. Characterization Of A Section 10(b) Claim

As this Court recognized in both *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976) and *Herman & MacClean v. Huddleston*, the right of action implied under Section 10(b) and Rule 10b-5 is a fraud claim. Congress adopted Section 10(b) to combat fraud (425 U.S. at 206), and the courts implied a private right of action under Section 10(b) to encourage and enable private enforcement of this significant anti-fraud provision of the federal securities laws (425 U.S. at 185); *Basic, Inc. v. Levinson*, 485 U.S. 224 (1988) ("a private cause of action exists for a violation of §10(b) and Rule 10b-5 and constitutes an essential tool for enforcement of the 1934 Acts' requirements"). While the provision was designed to combat a wide variety of conduct, the essence of that conduct is the same in every claim filed under this section: fraud in connection with the purchase or sale of securities. *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730 (1975). Section 10(b) claims do not involve multiplicity of different types of claims and thus one uniform federal standard is not necessary.

By contrast, civil claims for violation of the Racketeer Influenced And Corrupt Organizations Act ("RICO"),

18 U.S.C. §1964, may involve mail fraud, wire fraud, securities fraud, arson, bribery, theft, political corruption, breach of contract, fraud, conversation, tortious interference with business relations, misappropriation of trade secrets, unfair competition, usury and disparagement. *Agency Holdings*, 483 U.S. at 149. Moreover, RICO "enterprise" and "pattern of racketeering activity" are concepts unknown in the common law. *Id.* at 150. Thus, this Court concluded in *Agency Holdings* that because a multiplicity of limitations periods were applicable to the wide variety of conduct encompassed by RICO, "a uniform statute of limitations is required to avoid intolerable uncertainty and time-consuming litigation." *Id.* (Citation omitted.)

To identify the appropriate limitations statute for a 10b-5 claim, therefore, there is no need to evaluate the facts and legal theories of each claim. Because a 10(b) claim should always be characterized as a fraud claim, the characterization of the claim does not lead to the conclusion that state statutes of limitations "are an unsatisfactory vehicle for the enforcement of federal law." To the contrary, use of state limitations periods for Section 10(b) actions has not frustrated or interfered with the vigorous enforcement of the antifraud provisions of the federal securities laws upon which this Court and Congress have long insisted. *See, e.g., Basic*, at 231, 244-45.

As long as a Section 10(b) claim is consistently characterized as a fraud claim, and federal district courts look to a single state statute for the appropriate limitations period, the objectives of private enforcement of the federal securities laws will be met. Nothing in federal law or policy requires that all Section 10(b) actions be governed by a single, invariable limitations period. Moreover, the Third, Seventh and Second Circuits' *Data Access*, *Short*, and *Ceres* decisions have not achieved the stated goal of uniformity (*see, e.g., Data Access*, 843 F.2d at 1549). The use of the one year/three year statute of limitations will have an adverse effect upon the

enforcement of the securities laws, an effect which far outweighs any benefit which might result from the use of the various federal limitations periods created or selected by the Third, Seventh and Second Circuits.

This Court has not mandated the application of a single limitations period to causes of action for which Congress has not adopted an express statute of limitations. In *Wilson v. Garcia*, 471 U.S. 261 (1985), this Court held that state law causes of actions were more analogous to Section 1983 claims than federal causes of action, and therefore applied a limitations period drawn from state law. This Court further concluded that "federal interests in uniformity, certainty and the minimization of unnecessary litigation" favored the selection, in each state, of "the one most appropriate statute of limitations for all § 1983 claims." 471 U.S. at 275.

The Ninth Circuit recently rejected a request for *en banc* review of its prior decisions in *Davis v. Birr, Wilson & Co.*, 839 F.2d 1369 (9th Cir. 1988) and *Volk v. D.A. Davidson & Co.*, 816 F.2d 1406 (9th Cir. 1987). In *Davis* and *Volk*, the Ninth Circuit reaffirmed the selection of the single limitations period in each state for common law fraud for Section 10(b) claims. *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990). The Ninth Circuit further concluded in *Nesbit* that this Court's opinions in *Wilson* and *Agency Holding* "do not compel a reassessment and reversal of our position." *Id.*

Were courts to apply a single statute of limitations to all Rule 10b-5 claims arising within a state, much of the unnecessary litigation complained about in *Data Access*, *Short*, and *Ceres* would be cured. While the limitations period for Rule 10b-5 claims may vary from state to state, it is a simple

matter to determine the period within each state.[5] Uniformity within each state will be achieved without violating this Court's precedents and without severely limiting Rule 10b-5 claims.

B. The One-Year/Three Year Rule Does Not Provide A "Closer Analogy" To Section 10(b) Than Available State Law Fraud Statutes

Relying upon *Data Access*, *Short*, and *Ceres*, petitioner asks this Court to apply to Section 10(b) claims "a uniform federal statute of limitations — the one-year/three-year period contained in most of the express remedy provisions of the federal securities laws." Petitioner's Brief at 32. Petitioner suggests that "every one" of the express rights of action in the 1933 and 1934 Acts "is governed by an identical limitations period" and that these express rights of action provide a "far closer analogy" to Section 10(b) than any state law alternative. Because petitioner's assumptions are incorrect, so is its conclusion.

First, virtually all of the express remedies in the 1933 and 1934 Acts to which non-tollable limitations periods apply are not fraud claims. *Hochfelder*, 425 U.S. at 208, 209 n.28. *See also* Respondents' Brief at §III A. Second, each of the express rights of action in the 1933 and 1934 Acts is governed by a different statute of limitations,[6] and the limitations period crafted by the Third Circuit in *Data Access* is different still.

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[5] NASCAT agrees with respondents that common law fraud provides the "closest analogy" to Section 10(b) and therefore the state limitations period for common law fraud should apply to Section 10(b) claims.

[6] [C]lose examination of the various express limitations periods in [the 1933 and 1934] Acts reveals that no two are identical.

(footnote continues)

Third, this Court has already rejected the "closer analogy" argument. Application of a one-year/three-year limitations period to 10b-5 claims conflicts with this Court's decisions in *Hochfelder* and *Huddleston*, which decisions (in

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(footnote continued)

Section 13 of the 1933 Act provides the limitation periods for actions brought under Securities Act sections 11 and 12. For actions under section 11, the limitations period is one year from discovery of the true facts, or after discovery should have been made by the exercise of reasonable diligence, but no more that three years after the security was bona fide offered to the public. The limitations period for section 12(1) actions is one year after the "violation," but no more than three years after the security was bona fide offered to the public. The limitations period for section 12(2) actions is one year from discovery of the true facts, or after discovery should have been made by the exercise of reasonable diligence, but no more than three years after the "sale."

The 1934 Act contains statutes of limitation for the express civil causes of action under sections 9, 16, 18, and 29. The limitations period for actions brought under section 9(e) is one year from discovery of the facts constituting the cause of action, but no more than three years after "violation" of the section. A claim under section 16(b) is in the nature of a derivative action on behalf of the issuer, and the outside limit on commencing an action is two years after the insider realized a "short-swing" profit. The limitations period for violations of section 18(c) is one year from discovery of the facts constituting the cause of action, but no more than three years after the "cause of action accrued." The limitation period for a right of rescission under section 29 is one year after discovery that the purchase or sale of the security involved a violation of the Act, but no more than three years after the "violation."

The Third Circuit was deceived by the similarities among all these limitation periods and overlooked their significant differences. Only the limitation periods in the 1933 Act begin running from the time "discovery should have been made by the exercise of reasonable diligence. . . . " Presumably, the one year from discovery rules in the 1934 Act start to run not when the plaintiff should reasonably have been placed on inquiry, but only after the plaintiff has *actual notice* of *facts* that make up the violation. Because the Third Circuit never recognized this distinction, it purported to adopt both types of rules and never clarified whether it would impose a reasonable diligence standard on plaintiffs.

(footnote continues)

Hochfelder, to impose a scienter requirement on 10b-5 claims and in *Huddleston*, that the express liability provisions of the Acts and 10b-5 actions were not mutually exclusive) were both based in large part upon an assumption that the limitations period in a Section 10(b) case was longer than the limitations periods applicable to the express rights of action in the 1933 and 1934 Acts. *Hochfelder*, 425 U.S. at 210 n.29;[7] *Huddleston*, 459 U.S. at 384 n.18.

(footnote continued)

In addition, the three year outside limits of some of the express periods begin to run from the date of "sale," whereas others run from the date of the "violation" or from the "accrual of the claim." The Third Circuit undertook no analysis of these distinctions and simply adopted the rules using the "violation" as the starting point. In 10b-5 litigation, however, the time of the "violation" need not equate with the time of the sale." For example, in actively traded securities, a corporation may issue a press release containing materially false and misleading representations as to its financial condition. A month or more later, an investor may buy shares of that corporation's stock in reliance on the previously issued press release. Arguably, the "violation" occurred at the time the press release was issued, but the "sale" did not occur for another month, and the investor's cause of action could not have "accrued" until he purchased the stock. The Third Circuit made no effort to clarify which of these various periods it was adopting, nor did it state why it chose a three year period running from the violation rather than the sale.

Guin, *supra* note 1, at 564-65 (citations omitted).

[7] In *Hochfelder*, the Securities and Exchange Commission urged this Court to adopt a negligence standard of liability for Section 10(b) claims similar to the standards for claims brought under Section 11 and 12 of the 1933 Act. The Court carefully reviewed and compared Section 10(b) and Sections 11 and 12 and rejected the Commission's argument, stating that the claims under the 1933 Act which contain a negligence standard are subject to "significant procedural restrictions not applicable under §10(b)." 425 U.S. at 208-09. In reaching this conclusion, the Court explicitly referred to the differences between the statutes of limitations applicable to 1933 Act claims and Section 10(b) claims as being one of the significant procedural restrictions. The Court stated:

(footnote continues)

Fourth, the imposition of a non-tollable one-year/three-year statute of limitations upon Section 10(b)'s private right of action is contrary to this Court's directive to interpret and construe the federal securities laws flexibly in order to effectuate the "broad remedial purposes" of those laws. *Huddleston*, 459 U.S. at 386. Unlike the current precedent of this Court requiring the use of state limitations periods, application of a one-year/three-year period to 10b-5 claims would severely restrict the commencement of such claims (*see infra* at §§I.D. and I.E.), and thereby hinder this Court's oft-stated objective of facilitating and encouraging the private enforcement of the federal securities laws. *Basic*, 485 U.S. at 231, 244-45. The one-year/three-year, therefore, does not provide a "closer analogy" to Section 10(b) than state law.

C. Federal Policies At Stake And The Practicalities Of Litigation Do Not Make The One-Year/Three-Year Rule A More Appropriate Vehicle For Interstitial Lawmaking

The Ninth Circuit has refused to follow the Third, Seventh and Second Circuits which have decided two issues now presented in this case. First, the Third, Seventh and Second Circuits have each held that instead of applying a state statute of limitations to a claim brought pursuant to Section 10(b) of the 1934 Act, each circuit would apply a federal, albeit different, one-year/three-year statute of limitations. Second, each circuit has held that no tolling of the limitations period would be permitted in this Section 10(b) fraud action. Both holdings

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(footnote continued)

> Since no statute of limitations is provided for civil actions under §10(b), the law of limitations of the forum State is followed as in other cases of judicially implied remedies. *See Holmberg v. Armbrecht*, 325 U.S. 392, 395, 66 S. Ct. 582, 584, 90 L.Ed. 743, 746 (1946), and cases cited therein. Although it is not always certain which state statute of limitations should be followed, such statutes of limitations usually are longer than the period provided under §13. 3 Loss, *supra*, n.17 at 1773-1774. . . .

425 U.S. at 210 n.29.

contravene explicit rulings of this Court and both holdings create clear conflicts among the circuits (and even among the Third, Seventh and Second Circuits).

The Court is, of course, aware of the crucial role that private actions under Section 10(b) and Rule 10b-5 play in enforcement of the federal securities laws. Recently, this Court reemphasized that "a private cause of action . . . for a violation of §10(b) and Rule 10b-5 . . . constitutes an essential tool for enforcement of the 1934 Act's requirements." *Basic*, 485 U.S. at 231. In adopting the *Basic* "fraud-on-the-market" presumption of reliance for Section 10(b) class actions, the Court likewise reminded us of the vital role that class actions play in enforcing the antifraud provisions of the securities laws. *Id* at 243-44. No question may be more important to the maintenance of a cause of action and therefore to the private enforcement of the federal securities laws, than the statute of limitations applicable thereto. Because venue is national in securities fraud class actions, the one-year/three-year rule which fixes the limitations period for Section 10(b) claims at one year after the discovery and a maximum of three years after the occurrence, accrual, sale or a *bona fide* offering (depending on the rule or circuit), has significant practical implications for the conduct of private securities fraud class actions throughout the United States.

D. The One-Year/Three-Year Statute Is Non-Tollable And Eliminates For The First Time The Equitable Tolling Of A Limitation Period Applicable To A Fraud Class

In issuing its decisions prohibiting tolling of the newly fashioned one-year/three-year limitations periods in cases of securities fraud, the Third, Seventh and Second Circuits failed to adhere to this Court's precedents that "read into every federal statute of limitation" the equitable doctrine of

fraudulent concealment.[8] *Holmberg v. Armbrecht*, 327 U.S. 392, 397 (1946). For over a century, this Court has required that a tolling provision be appended to all limitations periods, applicable to lawsuits sounding in fraud, to the end that "no man may take advantage of his own wrong." *Glus v. Brooklyn Eastern District Terminal*, 359 U.S. 231, 232 (1959).

In an unbroken line of cases decided over the past 115 years, this Court has consistently and without deviation required that equitable tolling be read into all limitations periods governing causes of action sounding in fraud. This in itself is not surprising, since by its very nature fraud in all its forms is self-concealing. Its victims by definition are unaware of their status when the fraud is committed, and remain in ignorance as long as its perpetrators can conceal their wrongdoing. Tolling the applicable statute of limitations is thus the only mechanism by which a cause of action to redress the injury can be preserved. As this court explained over a century ago, "[t]o hold that by concealing a fraud, or by committing a fraud in a manner that it concealed itself until such time as the party committing the fraud could plead the statue of limitations to protect it, is to make the law which was designed to prevent fraud the means by which it is made successful and secure." *Bailey v. Glover*, 88 U.S. 342, 349 (1875). In *Exploration Co. v. United States*, 247 U.S. 435, 449

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[8] In addition to non-tolling, this rule is also objectionable because it requires filing of a Section 10(b) claim within one year from initial or "constructive" discovery of the fraud. In many cases, that will simply not be enough time for defrauded investors to determine the parameters, participants and details of the fraud sufficient to satisfy Rules 9(b) and 11 of the Federal Rules of Civil Procedure. This is particularly important today, as the complexity and size of frauds has increased and grown, and as frauds now often include not only primary defendants, but legal and accounting professionals as well. While the initial scope of a fraud and its perpetrators may be apparent within one year, it is often the case that the magnitude of the fraud and those involved are not fully known until many years later.

Even the Securities Exchange Commission requires, on average, 2.25 years to complete its fraud investigations. SEC Amicus Brief at 30.

(1918), this Court reaffirmed "the rule . . . that statutes of limitations to set aside fraudulent transactions shall not begin to run until the discovery of the fraud." More recently, in *Holmberg v. Armbrecht*, 327 U.S. 392, 397 (1946), this Court again had occasion to hold that "the old chancery rule" of equitable tolling "is read into every federal statute of limitations."

"Statutes of limitations are primarily designed to assure fairness to defendants." *Burnett v. New York Central R.R.*, 380 U.S. 424, 428 (1965). Prompted by "considerations deeply rooted in our jurisprudence," "in cases where the plaintiff has refrained from commencing suit during the period of limitations because of inducement by defendant, or because of fraudulent concealment, this Court has not hesitated to find the statutory period tolled or suspended by the conduct of the defendant." *American Pipe & Construction Co. v. Utah*, 414 U.S. 538, 559 (1974). *See Board of Regents v. Tomanio*, 446 U.S. 478, 487-88 (1980).

The Third Circuit's *Data Access* decision squarely holds that "the proper period of limitations for a complaint charging violation of Section 10(b) and Rule 10b-5 is . . . in no event more than three years after [the] violation." 843 F.2d at 1550. This is error. In failing to adhere to this Court's precedents that tolling is mandatory in all cases of fraud, the Third Circuit created an unwarranted exception to the "universal rule" (*Exploration Co. v. United States*, 247 U.S. at 449) that tolling is read into every limitations period governing claims that sound in fraud.

The practical effect of the adoption of a non-tollable one-year/three-year statute of limitations will be to encourage securities law violators to conceal their wrongdoing for the period of time required to extinguish all civil Section 10(b) claims that would otherwise be brought against them. Such concealment is often not difficult since the perpetrators of

stock fraud schemes are likely to be skilled and highly motivated businessmen with exclusive knowledge of the facts surrounding their conduct, while their victims are public shareholders and investors who, in ignorance of the fraud, have relied on the integrity of the price of their stock set by the workings of the impersonal securities market. *See Basic*, 485 U.S. at 245-46.

Likewise, imposition of an absolute three-year cut-off of the right to sue under Section 10(b), as required by the *Data Access* decision, flies in the face of what the Court again recently recognized as "the Congressional policy embodied in the 1934 Act" of "facilitating Rule 10b-5 litigation." *Basic*, 485 U.S. at 245. Contrary to "the congressional policy favoring private suits as an important mode of enforcing federal securities statutes" (*Pinter v. Dahl*, 486 U.S. 622, 633 (1988)), what the *Data Access* decision promises to achieve is stultification of Rule 10b-5 litigation and absolute immunity from suit, from both private plaintiffs and from the Securities and Exchange Commission, for all who successfully conceal their fraud for three years.

Until the *Data Access* decision, the law in every circuit was that the running of the limitations period applicable to Section 10(b) securities fraud actions must be suspended until the fraud is, or with the exercise of reasonable diligence should have been discovered. *Holmes v. Bateson*, 583 F.2d 542, 561 (1st Cir. 1978); *Klein v. Shields & Co.*, 470 F.2d 1344, 1346 (2d Cir. 1972); *Tobacco & Allied Stocks, Inc. v. Transamerica Corp.*, 244 F.2d 902, 903 (3d Cir. 1957); *Newman v. Prior*, 518 F.2d 97, 100 (4th Cir. 1975); *Breen v. Centex Corp.*, 695 F.2d 907, 911 (5th Cir. 1983); *Herm v. Stafford*, 663 F.2d 669, 682 (6th Cir. 1981); *Sperry v. Barggren*, 523 F.2d 708, 710 (7th Cir. 1975); *Harris v. Union Electric Co.*, 787 F.2d 355, 360 (8th Cir.), *cert. denied*, 479 U.S. 823 (1986); *Volk v. D.A. Davidson & Co.*, 816 F.2d at 1412; *State of Ohio v. Peterson, Lowry, Rall, Barber & Ross*, 651 F.2d 687, 691-92 (10th Cir.), *cert. denied*, 454 U.S. 985

(1981); *Kennedy v. Tallant*, 710 F.2d 711, 716 (11th Cir. 1983); *Wachovia Bank & Trust Co. v. Nat'l Student Marketing Corp.*, 650 F.2d 342, 349 (D.C. Cir. 1980), *cert. denied*, 452 U.S. 954 (1981). The Circuits' unanimous adherence to this principle stemmed from this Court's insistence on suspending the limitations period for victims of a fraudulent scheme until their discovery of the fraudulent conduct, a rule that safeguards against the possibility that wrongdoers will escape the consequences of their actions by concealing their fraud until the statute of limitations has run.

The Third Circuit did not acknowledge this Court's precedents applying this "universal rule." *Exploration Co. v. United States*, 247 U.S. at 449. Nor did it acknowledge that its decision has created a conflict among the circuits on the point. Instead, without discussion or analysis, it held that its newly created "one-year/three-year" limitations period for Section 10(b) claims is "absolute" and not subject to tolling.

Rejection of the non-tollable, one-year/three-year rule is warranted to correct the Third, Seventh and Second Circuits' failure to adhere to this Court's precedents on the question of tolling, as well as to repair the damage to both private and governmental securities enforcement efforts created by the decision, which promises to reward fraudulent conduct by immunizing it from challenge if it can be concealed until expiration of the three-year outer limitations period created by the *Data Access* decision.

E. The One-Year/Three-Year Period Would Undermine The Private Enforcement Of The Securities Laws

The *Data Access*, *Short* and *Ceres* decisions eliminate a significant source of protection for defrauded investors who, as a result of the defrauder's efforts, do not learn of the fraud until long after the wrong has been perpetrated. The doctrines of equitable tolling and equitable estoppel have long been available to toll limitations periods when the fraud is concealed. *Stitt v. Williams*, [Current Transfer Binder] Fed. Sec.

L. Rep. (CCH) §95,647 (9th Cir. December 12, 1990). Availability and application of these doctrines serves to further two policies enunciated by this Court on repeated occasions throughout its history of reviewing and interpreting the 1933 and 1934 Acts: the flexible construction of the Acts to effectuate their remedial purposes, and the private enforcement of the securities laws. *Basic*, 485 U.S. at 231, 245-46; *Huddleston*, 459 U.S. at 386; *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 310, (1985). Eliminating these common law doctrines would have an adverse impact upon the ability of private plaintiffs to assert violations of the securities laws, and therefore upon the enforcement of those laws, encouraging those who would defraud to do so and to do so in a manner which disguises their wrongdoing until the non-tollable limitations period expires.

There are untold numbers of investors who would never have recovered at all had such a draconian limitations period been in place. Perhaps the most poignant example involves the purchasers of $2.25 billion of municipal bonds issued by the Washington Public Power Supply System ("WPPSS") between 1977 and 1981 to finance the construction of two nuclear power plants. The Supply System ceased constructing these power plants in 1982 and thereafter defaulted on the $2.25 billion bonds. On March 8, 1983, plaintiffs filed a class action alleging that defendants violated federal and state securities laws by making materially false and misleading statements to sell the bonds to the public. *See In re Washington Public Power Supply System Securities Litigation*, 823 F.2d 1349 (9th Cir. 1987). Following hard-fought litigation, the case was settled for in excess of $700 million.

The massive harm caused by the WPPSS bond fraud would never have been remedied for thousands of investors had the non-tollable *Data Access* limitations period been in effect. Under such a limitations period, anyone who purchased a WPPSS bond prior to March 8, 1980 (three years prior to the filing of plaintiffs' WPPSS complaint) would have

been barred from bringing suit to remedy the harm caused by the ongoing six-year fraud. Instead, this purchaser would have been expected to bring suit at a time when the fraud was fully concealed and in the face of the strictures imposed upon counsel by Rule 11 of the Federal Rules of Civil Procedure, while defendants continued to sell WPPSS bonds to the public for at least another three years. In real terms, pre-March 8, 1980 purchasers of $1.5 billion of WPPSS bonds would have never recovered for defendants' violations of the federal securities laws.

Similarly, victims of the most egregious acts of securities fraud, such as long-running pyramid or Ponzi schemes, would have no remedy under the *Data Access* "solution" so long as defendants could hide the true facts from investors for three years. Indeed, under *Data Access*, investors in multi-offering limited partnership schemes are particularly disenfranchised: these schemes typically run over a course of several years before collapse. Because the investment programs themselves are long term, early as well as late investors lose everything upon the program's demise. The federal courts have consistently recognized that *all* investors defrauded in a long-term Ponzi scheme should have recourse under Rule 10b-5. For example, under a *Data Access* rule, most of the 3,000 investors in the twelve-year, multi-offering Ponzi scheme described in *In re Home-Stake Production Co. Securities Litigation*, 76 F.R.D. 351, 358-61 (N.D. Okla. 1977); the 3,000 investors in the 40-partnership, four-year Ponzi scheme described in *Roberts v. Heim*, 670 F. Supp. 1466, 1473-75 (N.D. Cal. 1987); and the nine-year,multi-offering oil and gas Petro-Louis Ponzi scheme described in *Bresson v. Thomson McKinnon Securities Inc.*, 118 F.R.D. 339, 341 (S.D.N.Y. 1988), would have been left without recourse under the federal securities laws. Instead, these investors sustained their claims and ultimately recovered damages, via settlement or judgment.

The unfairness of this rule and current events dictate a different result. If a one-year/three-year rule is adopted by this Court, victims of the most visible frauds of our day may be denied recovery for their injuries under the federal securities laws. The scandals involving Drexel Burnham Lambert and Michael Milken include transactions which span the 1980's and it was not until the September 7, 1988 filing of the SEC's civil indictment naming Drexel, Milken and others that the wrongdoing of Drexel and Milken was first publicly exposed. *SEC v. Drexel Burnham Lambert, Inc., et al.*, Civil Action No. 88 CIV 6209 (S.D.N.Y. September 7, 1988).[9] Under the one-year/three-year rule, investors harmed by Drexel or Milken's conduct prior to September 1985 will be precluded from asserting a Section 10(b) claim.[10]

The most recent example of the inequitable and arbitrary adverse effect of the application of a non-tollable, one-year/three-year statute of limitations to a Section 10(b) claim is the district court's October 19, 1990 decision in *In re VMS Securities Litigation*, 89 C 9448 (N.D. Ill.) (Slip Op. at 24). Between 1984 and 1988, in a series of public offerings, VMS sold limited partnerships in VMS entities that developed commercial real estate. *Id.* at 5-10. On December 22, 1989, plaintiffs filed suit, alleging that defendants had materially misrepresented real estate values, office space projection and the structure of the partnership interests, thereby violating,

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[9] Pursuant to Rule 201 of the Federal Rules of Evidence, NASCAT requests that the Court take judicial notice of the judicial records referred to in this section.

[10] Similarly, the Sixth Amended Complaint in *Shields v. Keating, et al.*, MDL 834 (D. Ariz. 1989), commonly known as the American Continental/Lincoln Savings Securities Litigation, encompasses more than a three-year period (January 1, 1986 through April 14, 1989) and perforce under a one-year/three-year rule, many of the defrauded purchasers of American Continental securities would not be permitted to pursue Section 10(b) claims against, *inter alia*, Charles Keating, other officers and directors of American Continental and American Continental's auditors and counsel.

inter alia, Section 10(b). By adopting the one-year/three-year rule, the court eliminated the Section 10(b) claims of individuals who purchased approximately $475 million of limited partnership interests from the defendants during a four-year period in which defendants sold approximately $1 billion of such interests. *Id.* This wholly unfair and arbitrary result occurred even though (i) all of the VMS plaintiffs were victims of the defendants' same, ongoing, wrongful course of conduct; and (ii) the VMS plaintiffs did not become aware of their claims until November 14, 1989. *Id.* at 25.

II. THE FIVE-YEAR STATUTE OF LIMITATIONS IN SECTION 20A OF THE SECURITIES ACT OF 1934 IS "MORE ANALOGOUS" THAN THE ONE-YEAR/THREE-YEAR PERIOD AND WOULD PROMOTE, RATHER THAN EVISCERATE, THE PRIVATE ENFORCEMENT OF THE SECURITIES LAWS

If this Court nevertheless concludes that the limitations period for Rule 10b-5 claims should be found in federal, not state law, we have demonstrated above why application of the limitations periods found in Section 13 of the 1933 Act or Sections 9 and 18 of the 1934 Act would be inappropriate. Rather, this Court should apply the five-year limitation period of Section 20A of the 1934 Act.[11] Section 20A, known as the Insider Trading and Securities Fraud Enforcement Act

[11] NASCAT joins in the arguments of the Securities and Exchange Commission in support of the application of Section 20A's statute of limitation to 10b-5. *See* SEC Amicus Brief at 21-34. NASCAT does not, however, agree with the SEC's position that equitable tolling of Section 20A should not be permitted. As Judge Easterbrook noted in the Seventh Circuit's *Short* decision, there is nothing in the legislative history to suggest that Section 20A is other than a traditional, ordinary statute of limitations, without the restrictive, three-year language of the other limitation periods in the 1933 and 1934 Acts. 908 F.2d at 1391. For the reasons set forth *supra* in §§I.D.-I.E., equitable tolling should apply to Section 20A's limitations period.

of 1988, was passed to "augment enforcement of the securities laws, particularly in the area of insider trading." H.R. Rep. No. 910, 100th Cong., 2nd Sess. 26, reprinted in 1988 U.S. Code Cong., & Admin. News 6063, at 7. It provides express civil liability for "contemporaneous traders" of those trading on inside information and was developed to complement Rule 10b-5 claims based on insider trading. *Id.* at 157. At the time it was passed, Congress did not create a provision that contained an express cause of action for persons other than "contemporaneous traders" because it did not want to freeze the law and instead wanted "to give the courts leeway to develop implied private rights of action in an expansive fashion in the future." *Id.* at 27. Thus, Section 20A not only represents Congress' latest thoughts on limitations periods, but was passed against the backdrop of various interpretations of Rule 10b-5 and was crafted so as to ensure that the courts had leeway to develop Rule 10b-5 actions, which could overlap with Section 20A claims, in an "expansive fashion in the future." Accordingly, if Congress intended any federal limitations period to apply to Rule 10b-5 claims, this limitations period would be the five-year statute recently enacted (with full knowledge of the development of the law regarding Rule 10b-5), rather than the system created over fifty years ago.[12]

[12] In *Short*, the Seventh Circuit argues that the five-year limitations period in Section 20A is too long because "prudent investors almost always can sniff out fraud (or enough smoke to justify litigation) within three years. Section 13 cuts off only the claims of the most trusting or somnolent. . . . " 908 F.2d at 1392. There is *no* empirical evidence supporting this insensitive view, and, as it intentionally leaves the most defenseless group of investors without a remedy under the securities laws, it should not be given much weight. Moreover, under Rule 9(b) of the Federal Rules of Civil Procedure, investors are not *permitted* to file fraud allegations under Rule 10b-5 simply because they suspect fraud or can smell a whiff of "smoke." To do so would suggest sanctions under Rule 11 of the Federal Rules of Civil Procedure.

III. ANY STATUTE OF LIMITATIONS WHICH MAY BE SELECTED FROM FEDERAL LAW AND APPLIED TO SECTION 10(b) CLAIMS SHOULD NOT BE RETROACTIVE

Even if the Court decides to apply the *Data Access* one-year/three-year limitations period to Rule 10b-5 claims, it should not do so retroactively.

In *Chevron Oil Co. v. Huson*, 404 U.S. 97, 106-07 (1971), the Supreme Court held that a newly announced rule of law should not be applied retroactively when (1) the new rule overrules clear past precendent on which litigants may have relied; (2) its purpose and effect would not be substantially furthered by retroactive application; and (3) imposing the rule retroactively would produce inequitable results because it would impose hardship or prejudice. Although the majority in *Data Access* did not decide the issue of retroactivity, a strong dissent by three judges on the *en banc* panel applied the *Chevron Oil* test, and concluded that the one-year/three-year rule should not be applied retroactively. *Data Access*, 843 F.2d at 1552-53 (Judge Seitz dissenting). *See also In re National Smelting of New Jersey, Inc. Bondholders' Litigation*, 722 F. Supp. 152, 158-60 (D.N.J. 1989) (refusing to apply the one-year/three-year rule retroactively).

Application of the *Chevron Oil* test inevitably leads to the conclusion that the *Data Access* rule should not be applied retroactively. First, application of the *Data Access* rule would be a clear departure from precedents in all circuits upon which plaintiffs may have relied, especially since plaintiffs would be deprived of their right to sue because the statute had run prior to the time they had any reason to believe that the fraud was perpetrated. Second, as set forth above in §I.E., retroactive application would deprive thousands of defrauded investors of any remedy whatsoever. While this certainly would be a fortuitous event for the defendants in the affected actions, it would do nothing to advance the purposes of the securities laws. Moreover, only applying the new rule

prospectively would not significantly further or retard the policy objectives underlying the *Data Access* decision. Third, it would be inequitable to deprive plaintiffs of their right to bring Section 10(b) claims when they did not know that the defendants would be able to avoid liability for any wrongdoing simply be hiding the true facts for three years. This would be a gross injustice, since plaintiffs would suddenly be exposed to fraud without the protection offered by the equitable tolling doctrine. As this Court stated in *Chevron Oil*, "[i]t would . . . produce the most 'substantial inequitable results' to hold that [plaintiff] 'slept on his rights' at a time when he could not have known the time limitations that the law imposed upon him . . . [N]onretroactive application here simply preserves his right to a day in court." 404 U.S. at 108 (citation and footnote omitted).

Recently the Third Circuit refused to apply its *Data Access* decision retroactively in *Gruber v. Price Waterhouse*, 911 F.2d 960 (3d Cir. 1990). In *Gruber*, the Third Circuit found that components one and three of the *Chevron* test "mandate prospective application in cases where a new period of limitations replaces a well-settled statute since it would be inequitable to change the rules in midstream when clear precedent had been relied upon." *Id.* at 968. The *Gruber* decision was recently followed in *Haumann v. Illinois Power Co., et. al*, Civil Action No. 89-1130 (C.D. Ill. December 4, 1990). The court concluded in *Haumann* that the Seventh Circuit's opinion in *Short* overruled clear past precedent upon which the litigants may have relied, and that to apply the *Short* decision retroactively would produce substantial inequitable result. Transcript of Hearing at 4, 8.

Accordingly, this Court should not apply the *Data Access* one-year/three-year rule retroactively.

IV. CONCLUSION

Application of a non-tollable, one-year/three-year statute of limitations to Section 10(b) claims would hamper the

effectiveness of the Section and hinder this Court's frequently-repeated objective of the facilitation and encouragement of private enforcement of the federal securities laws. Accordingly, the decision of the Ninth Circuit Court of Appeals should be affirmed.

If this Court concludes that it must look to federal law for a Section 10(b) limitations period, then the Court should adopt the limitations period contained in Section 20A of the 1934 Act. Section 20A's limitations period, with equitable tolling, is more analogous to Section 10(b) than the one-year/three-year rule and will maintain this Court's long line of precedents which support the private enforcement of the securities laws.

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No. 90-333

In The

Supreme Court Of The United States

October Term, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, et al.,
Respondents.

On Writ of Certiorari to the United States
Court of Appeals for the Ninth Circuit

BRIEF OF BOND INVESTORS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF RESPONDENTS

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No. 90-333

In The

Supreme Court Of The United States

October Term, 1990

LAMPF, PLEVA, LIPKIND, PRUPIS & PETIGROW,
Petitioner,

v.

JOHN GILBERTSON, et al.,
Respondents.

On Writ of Certiorari to the United States
Court of Appeals for the Ninth Circuit

BRIEF OF BOND INVESTORS ASSOCIATION AS AMICUS CURIAE IN SUPPORT OF RESPONDENTS

PRELIMINARY STATEMENT

Pursuant to Rule 37 of this Court, the Bond Investors Association, Inc. ("BIA") submits this brief as amicus curiae in support of the Respondents.[1]

The issue in this case is what statute of limitations should govern actions under Section 10(b) of the Securities Exchange Act of 1934, 15 U.S.C. § 78j(b) and Rule 10b-5 thereunder, 17 C.F.R. 240.10b-5. This Court is asked to decide whether courts should continue the practice previously recognized by this Court in *Ernst & Ernst v. Hochfelder*, 425 U.S. 185, 210 n. 29 (1976) and *Herman & MacLean v. Huddleston*, 459 U.S. 375, 384 n.18 (1983) of borrow-

[1]Written consents signed by all parties have been filed with the Clerk's office.

ing limitations periods from analogous state statutes, or whether 10b-5 claims should be governed by a limitations period borrowed from some federal statute. If the Court adopts a limitations period from some federal cause of action, additional issues will be presented, such as (1) which federal statute should be borrowed, (2) whether federal equitable tolling and equitable estoppel doctrines are applicable to the chosen limitation period, and (3) whether the new limitations period will be applied retroactively.

The BIA urges the Court to continue the practice of adopting state limitations periods, but to do so on a statute-by-statute basis. If the Court decides to adopt a federal limitations period, the BIA urges the Court to adopt either the five-year limitations period drawn from Section 20A of the Securities Exchange Act of 1934, 15 U.S.C. § 78t-1, coupled with equitable tolling, or the three-year from discovery rule applicable to the 10b-5 clone contained in the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701, et seq.

INTEREST OF AMICUS CURIAE

The BIA is a 14,000 member non-profit corporation that provides information to holders of municipal and corporate bonds. BIA was founded in 1984 to assist in providing information to bondholders victimized by the $2.25 billion Washington Public Power Supply Systems ("WPPSS") municipal bond default, and has since expanded its informational services to holders of corporate and other municipal bonds. BIA, which maintains the only comprehensive database on municipal and corporate bond defaults, provides default information and analysis to electronic data services and the public via a monthly newsletter. The information maintained by BIA on defaulted bonds is a unique resource and is regularly used by the SEC, Congress, the General Accounting Office, the Federal Reserve Bank and the media. Much of the statistical information cited by the SEC in its reports on the WPPSS default was obtained from BIA.[2]

[2]See Report of the Securities and Exchange Commission on the Regulation of Municipal Securities, [1988-89 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 84,325 (Sept. 22, 1988); Securities Exchange Act Release No. 26100, [1988-89 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 84,326 (Sept. 22, 1988); Staff Report of the Investigation in the Matter of Transactions in Washington Public Power Supply System Securities, [1988-89 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 84,326 (Sept. 22, 1988).

BIA has a substantial interest in the matters before this Court because adoption of a short limitations period or a statute of repose for Rule 10b-5 actions would deprive defrauded bond purchasers of the only meaningful avenue of recovery for deliberate frauds directed against them. None of the express rights of action in the 1933 and 1934 Acts are applicable to tax-exempt municipal bond frauds, and because of the structure and nature of municipal bond financings, the short limitations period urged by Petitioner would deny a remedy to defrauded bond buyers.

SUMMARY OF ARGUMENT

In the last ten years, there have been at least 750 municipal bond defaults totalling over $9,200,000,000 in principal amount.[3] When industrial development or revenue bonds are issued to finance the construction or improvement of a project, a portion of the bond sale proceeds are held in capitalized interest and debt service reserve funds in order to pay interest on the bonds during construction and start-up of the project. Even if the bond issue is a sham, bondholders often have no reason to suspect fraud for several years because they will receive their scheduled interest payments from the reserve funds. Because the express rights of action in the 1933 and 1934 Acts are inapplicable to tax-exempt municipal bond frauds, and discovery of such frauds is often impossible as a practical matter within a three-year statute of repose, such a short limitations period would deny a remedy for securities fraud to purchasers of defaulted municipal bonds.

The BIA urges the Court to continue the traditional practice of borrowing state limitations periods. Unlike the cases in which this Court has looked to federal analogies to supply a limitations period, Congress has acquiesced in this practice in 10b-5 actions for over four decades, and decisions of this Court shaping the law of Rule

[3]Laing, *The New Junk? Risks Are Rising in the Vast Municipal Bond Market*, Barron's, Oct. 29, 1990, at 10, col. 2. Photocopies of all newspaper and magazine articles have been lodged with this brief.

10b-5 have relied to a significant extent on the practice. If the Court does choose to abandon the traditional practice of applying state law limitations periods, BIA urges the Court to adopt the five-year limitations period enacted by Congress in the Insider Trading and Securities Fraud Enforcement Act of 1988[4] or the three-years from discovery limitations period found in the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701 et seq. Both alternatives provide better analogies to 10b-5 actions than the periods suggested by the Petitioner.

ARGUMENT

I. MOST SECURITIES FRAUDS ARE NOT DISCOVERABLE WITHIN A THREE-YEAR STATUTE OF REPOSE

Like foxes piously guarding the chicken coop, the petitioning defendants ostensibly seek to add to the effectiveness of § 10(b) and Rule 10b-5 actions by urging the adoption of the limitations period created in *In re Data Access Sys. Sec. Litigation*, 843 F.2d 1537 (3d Cir.), *cert. denied*, 488 U.S. 849 (1988), which requires that 10b-5 actions be filed within one year from the date of discovery[5] of the fraud, but no more than three years after the "violation." (See Petitioner's Brief at 6). Under the guise of promoting the "effectiveness" of the Act, the defendants instead seek to emasculate 10b-5 actions by depriving defrauded investors of their right to sue. Simply put, defrauded investors in the unregulated municipal bond market cannot reasonably be expected to discover the sort of deliberate fraud prohibited by Rule 10b-5 within three years of the sale of the securities.

The municipal bond market is not an inconsequential aspect of the investment world. There are approximately $830 billion in face amount of municipal bonds currently outstanding,[6] more than three

[4]Pub. L. No. 100-704, § 5, 102 Stat. 4681 (adding Section 20A(a), 15 U.S.C. § 78t-1(a)).

[5]The Third Circuit did not directly address the issue in *Data Access*, but in *Gruber v. Price Waterhouse*, 911 F.2d 960, 964 n. 4 (3d Cir. 1990) that court held that its discovery rule is one year from actual, rather than inquiry, notice.

[6]Farrell, *Once Upon A Time, A Muni Was A Muni Was A Muni . . .*, Business Week, December 31, 1990, at 121, col. 1.

times the face amount of all corporate bonds in the market.[7] During the past decade, over $9 billion in municipal bonds have defaulted and the default rate is currently $1 billion per year.[8] Although the municipal bond market in years long past was dominated by institutional investors, in recent years increasing amounts of municipal bonds have been sold to individuals.[9] Many municipal bond purchasers are unsophisticated, elderly retirees,[10] some of whom may not fully appreciate the difference between general obligation bonds (which are backed by the full faith and credit of the municipal issuer)[11] and revenue bonds (the principal and interest of which are to be repaid from revenues of the financed project).[12]

[7]Laing, *The New Junk? Risks Are Rising in the Vast Municipal Bond Market*, Barron's, Oct. 29, 1990, at 10, col. 2.

[8]*Id.* See also Stevens, *Congress Urged to Ban Muni Issuers From Selling Conduit Bonds*, The Bond Buyer, May 8, 1990, at 1, col. 2; Boyle, *Defaults Leap 36.6% In The First Quarter, Investors Group Says; Two Issues to Blame*, The Bond Buyer, Ap. 5, 1990, at 1, col. 2; *Bond Defaults Rise in First Quarter*, The Commercial and Financial Chronicle, Ap. 4, 1990, page 15; Luxenberg, *Beware of Municipal Junk Bonds*, The New York Times, Dec. 11, 1988, at F6, col. 3.

[9]In addition, mutual funds, which are marketed primarily to individual investors, have increased their holdings of municipal bonds dramatically. Six years ago, 60 muni funds held only $13.2 billion in assets, but as of October, 1990, 190 muni funds now hold $68.7 billion of muni debt. Farrell, *Once Upon A Time, A Muni Was A Muni Was A Muni . . .*, Business Week, Dec. 31, 1990, at 121, col. 1. At the same time, however, credit ratings have been dropped on New York City, Philadelphia, and Massachusetts bonds, *Id.*, at 120, col. 3, and about half the states are taking in less revenue with which to repay their bonds than forecasted. *Id.* Philadelphia's credit rating has been lowered to CCC, one notch above "default." T. McCarroll, *City on the Brink*, Time, January 7, 1991, at 58.

[10]*In the Matter of Transactions in the Securities of the City of New York, Final Report*, [1979 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 81,936 (Feb. 5, 1979).

[11]Even general obligation bonds default and become the subject of SEC enforcement actions. Securities Exchange Act Release No. 26100, [1988-89 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 84,326, at 89,448 n. 1. Some municipal issuers' credit, even when it backs a bond, is not worth much, as was demonstrated by the New York City fiscal crisis and government bail-out in the 1970s. See *In the matter of Transactions in the Securities of the City of New York, Final Report*, [1979 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 81,936 (Feb. 5, 1979); *Friedlander v. City of New York*, 71 F.R.D. 546 (S.D.N.Y. 1976); *Spector v. City of New York*, 71 F.R.D. 550 (S.D.N.Y. 1976). Even today, cities such as Philadelphia are facing credit crunches and currently are "going through financial contortions to avoid defaulting on [their] GOs." Farrell, *Once Upon A Time, A Muni Was A Muni Was A Muni . . .*, Business Week, at 121, col. 1.

[12]Sing, *Simple Steps To Avoid Municipal Bond Scams*, The Los Angeles Times, Mar 18, 1989 § IV, at 3, col. 1.

Such so-called revenue bonds make up more than 60% of today's $830 billion bond market, and 70% of all new tax-exempt bond issues are revenue bonds.[13] Although revenue bonds nominally are issued by some governmental authority as a conduit, the moving force behind the issuance of revenue bonds is typically the private enterprise seeking the funds.[14]

Because the only source of funds to pay interest to bondholders is the revenue of a project not yet in service, a portion of the proceeds from the sale of the bonds is set aside to service the bond debt until the revenue stream is sufficient to do so. For example, if the bonds are used to finance the construction of a nursing home or retirement facility, it will be necessary to construct the project, market it and achieve a given occupancy level in order to generate the positive cash flow necessary to service the bond debt. The bond proceeds must provide sufficient funds to pay the interest on the bonds in addition to construction costs and other expenses during this construction and start-up period, which typically lasts several years. Accordingly, a portion of the proceeds from the sale of the bonds is usually allocated for "capitalized interest" and paid to the indenture trustee to be deposited into an interest- payment account. Additional funds, such as the "debt service reserve fund," are designed to provide funds to service the bond debt after the capitalized interest account is exhausted and to make up any shortfalls in the project's operating revenues in the event of a shortfall of revenues. See Guin & Donaldson, The Insider Trading and Securities Fraud Enforcement Act: Has Congress Supplied a Limitations Period Appropriate for Use in Private 106-5 Actions?, 47 Wash. &

[13]Farrell, *Once Upon A Time, A Muni Was A Muni Was A Muni . . .*, Business Week, Dec. 31, 1990, at 121, col. 1.

[14]See Hylton, *Junk Forecast: Wide Premiums*, The New York Times, Jan. 25, 1990, at D10, col. 3. Many states' laws allow developers to declare just about any parcel of land a special "taxing district, with their decision to float bonds rubber stamped by county commissioners. See Charlier, *Junk Munis; Many Tax-Free Bonds Are Going Into Default In Colorado Land Bust*, The Wall Street Journal, December 7, 1990, page 1, col. 6. The local commissioners have every incentive to cooperate with developers since the developers envision building new projects within the county or municipality with money raised from outsiders who will have no recourse against the municipality in the event of default. The lack of oversight coupled with high front-end fees is a ready-made breeding ground for fraud.

Lee. L. Rev. 541, 570 (Summer 1990) (hereinafter, "Guin & Donaldson").

Bond investors rarely have any inkling of even normal economic problems, much less fraud, until a coupon interest payment is missed.[15] Typically, interest is paid semi-annually. With the minimum eighteen to twenty-four month capitalized interest reserve fund, the first missed interest payment will not occur for at least twenty-four to thirty months after the initial closing of the bond issue and perhaps longer if the debt service reserve fund or some working capital reserve fund created with sources other than bond proceeds are utilized. See Guin & Donaldson, at 570-71. The database maintained by the BIA indicates that over the last ten years, the average time span between the issue date for municipal bonds which later defaulted and the date of default in the repayment of the bonds was 54.3 months (approximately 4.5 years). *Cf.* Staff Report on Transactions in the Marine Protein Corp. Ind. Dev. Revenue Bonds, [1979 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 82,049 (April 11, 1979) (bonds defaulted four years after issuance, SEC found deliberate fraud).[16] Accordingly, the earliest point at which bondholders reasonably can be expected to learn that anything at all is amiss with their investment would be near or after the expiration of the *Data Access* limitations period. *Id.*

The difficulty of discovering bond fraud is compounded by the fact that the municipal bond market is essentially unregulated. Municipal bonds are exempt from the registration requirements of the 1933 Act,[17] the periodic reporting requirements of the 1934 Act,[18] the Trust Inden-

[15]See Fritz, *X-Rated Bonds*, Forbes, Mar. 21, 1988, at 167, which reports that sometimes municipal bond trustees often do not report defaults at all. See also Ferris, *Trustee Data Should Be Put In Repository For Disclosure*, The Bond Buyer, April 4, 1988.

[16]In the *WPPSS* case, for example, because the proceeds of the bonds were to be used to finance the construction of nuclear power facilities, the construction period reserve funds lasted significantly beyond the three-year cut off of the *Data Access* rule. See, e.g., Staff Report of the Investigation in the Matter of Transactions in Washington Public Power Supply System Securities, [1988-89 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 84,327, at 89,461-462 (Sept. 22, 1988).

[17]§ 3(a)(2) of the 1933 Act, 15 U.S.C. § 77c(a)(2).

[18]§§ 3(a)(12), 12(a), 13(a), 14(a) and 16(a) of the 1934 Act, 15 U.S.C. §§ 78c(a)(12), 78l(a), 78m(a), 78n(a) and 78p(a).

ture Act Requirements,[19] and, generally, the registration requirements of blue sky laws in the state of issuance.[20] Therefore, there are no uniform requirements as to what information has to be provided to bondholders. In the typical revenue bond issue with a passive issuer, bondholders and would-be investors are dependent upon the indenture trustee, who has little budget for public dissemination of financial and other periodic reports, for information on the status of the project financed by the bonds. Individual trust indentures vary widely in any covenants they contain as to what information (if any) the project sponsor must furnish the indenture trustee, or the date as of which it must be furnished. Indenture trustees operating under a tax-exempt bond indenture generally are not privy to the information that would be required to be disclosed by 1934 Act reporting companies, and to the extent indenture trustees are in possession of any material information about the project, they often disclose such information only reluctantly, if at all.[21]

Even if the trustee does decide to notify the bondholder of the promoters' financial difficulties or of a default in the repayment of the interest and principal on the bonds, it will not necessarily put bondholders on notice of a possible fraud.[22] Projects financed by bond issues can fail for reasons having nothing to do with fraud and the potential defendants are likely to blame the default on unforeseen post-closing events. Since revenue bonds are secured by the project constructed with the bond proceeds, bondholders also do not know at the time of default whether they will suffer a loss on their investment, and if so, how much the loss will be. The project may remain open, close, be sold at foreclosure, be refinanced, or be foreclosed on. Guin & Donaldson, at 569-71.[23]

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[19]Trust Indenture Act of 1935, § 4(a)(4)(A), 15 U.S.C. § 77ddd(a)(4)(A).

[20]See, e.g., Uniform Securities Act § 402(a)(1), 1 CCH Blue Sky Law Reporter ¶ 5542.

[21]See J.E. Spiotto, *Defaulted Securities: The Prudent Indenture Trustee's Guide* (American Bankers Assoc. 1990).

[22]Another difficulty is caused by the fact that many bonds are held in "street name," and the beneficial owners of such bonds may receive any trustee notices very late if at all. Further, trust indentures rarely require trustees to mail regular reports or financial information to bondholders.

[23]One recently-published manual for indenture trustees even cautions trustees to advise the bondholders that it "may be in [their] best interests . . . to be patient and not to proceed immediately to litigation or other remedies." J.E. Spiotto, *Defaulted Securities: The Prudent Indenture Trustee's Guide*, at XII-14 (1990).

A three-year statute of repose will prevent 10b-5 actions from being a viable remedy for many defrauded investors or an effective deterrent to would-be malfeasors.[24] Because the express rights of action are inapplicable to municipal bond frauds, adoption of a short limitations period for Rule 10b-5 actions will leave defrauded bond purchasers with only inadequate state law remedies.[25] Such a result is inconsistent with the purpose of Rule 10b-5 because the federal securities statutes were enacted to rectify deficiencies in state law protection and to establish higher standards of conduct in the securities industry. *Herman & MacLean v. Huddleston*, 459 U.S. 375, 389 (1983); see *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186 (1963).[26]

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[24]The practical inability to discover fraud within three years is not peculiar to municipal bonds. Any financial fraud can be difficult to uncover, at least until the business folds. Similarly, garden variety "Ponzi schemes," in which the malfeasor induces the victim to invest with promises of high returns, which in fact, are paid only out of other investments, can be carried out as long as new investments can be obtained. In the classic Ponzi, the malfeasor pockets all of the invested funds not used to create the phoney "return." More often, the malfeasor makes the scheme more sophisticated (and more difficult to detect) by funneling a portion of the investments into actual business operations which create a phoney "return" by using investor funds to cover losses. This latter type of scheme can be virtually undetectable for an extended period of time because the investor, upon inquiry, can observe an actual, operating business. See, e.g., *Thousands Reportedly Hit by Ponzi Schemes - - Investors Bilked Out of More Than $750 Million*, L.A. Times, June 9, 1985, Part V, at 8; D. Akst, *How Barry Minkow Fooled the Auditors*, Forbes, October 2, 1989, at 126; Stern & Giltenan, *"Norma, Would I Do Anything to Hurt You?"*, Forbes, June 13, 1988, at 37; *The Whiz Kid Who Wasn't*, Time, January 25, 1988.

[25]*Cf. Woolf v. S.D. Cohn & Co.*, 521 F.2d 225, 227-28 (5th Cir. 1975), noting that the effectiveness of Rule 10b-5 is particularly important in the case of unregistered securities, such as municipal bonds and the limited partnership interests at issue here due to the lack of SEC oversight and publicly available information.

[26]Many defrauded investors, because of the small amount of their individual claims, rely on the class action device to seek redress. See *Deposit Guaranty Nat'l Bank v. Roper*, 445 U.S. 326, 338-39 (1980). However, a number of federal courts have held that state law rights of action brought as pendent claims to Rule 10b-5 actions are inappropriate for class action treatment. See, e.g., *Kirkpatrick v. J.C. Bradford & Co.*, 827 F.2d 718, 725 n. 6 (11th Cir. 1987). While BIA disagrees with those decisions, until this Court reverses their holdings, defrauded investors will have no practical means of redress if this Court adopts the short limitations period suggested by Petitioner. The limitations period will be too short to obtain redress under Rule 10b-5, and in at least some circuits, cheated investors will have no right to pursue a class action under common law theories.

II. STATE LIMITATIONS PERIODS, TEMPERED BY THE FEDERAL DOCTRINES OF EQUITABLE TOLLING AND EQUITABLE ESTOPPEL, SHOULD CONTINUE TO BE BORROWED FOR RULE 10b-5 ACTIONS

A. Data Access *Directly Conflicts with Supreme Court Pronouncements Regarding 10b-5 Limitations Periods*

1. Data Access *Conflicts With Supreme Court Decisions on 10b-5 Law Generally*

The *Data Access* approach is in direct conflict with this Court's decisions in the seminal Rule 10b-5 cases of *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976) and *Herman & MacLean v. Huddleston*, 459 U.S. 375 (1983). In *Hochfelder*, this Court stated:

> Since no statute of limitations is provided for civil actions under § 10(b), the law of limitations of the forum state is followed as in other cases of judicially implied remedies. See *Holmberg v. Armbrecht*, 327 U.S. 392, 395 (1946). Although it is not always certain which state statute of limitations should be followed, such statutes of limitations usually are longer than the [one-year/three-years] period provided under § 13 [of the Securities Act of 1933].

425 U.S. at 210 n. 29.

Not only did this Court in *Hochfelder* recognize the applicability of this traditional borrowing rule to 10b-5 actions, that conclusion was important to its ultimate ruling that scienter is an element of the cause of action. The Court held that it would be appropriate to impose a scienter requirement in Rule 10b-5 actions, among other reasons, because plaintiffs in 10b-5 actions are not hampered by the short three- year statute of repose placed on certain of the express securities rights of action.[27]

In *Huddleston*, this Court similarly stated,

[27]If this Court reverses itself and adopts some previously-existing federal limitations period for 10b-5 actions, it should revisit its imposition of a scienter requirement in Rule 10b-5 actions as well.

> [C]ourts [in Rule 10b-5 actions] look to the most analogous statute of limitations of the forum state, which is usually longer than the [one-year/three-years] period provided for Section 11 actions.

Id., at 384 n.18. The Court again relied to a significant extent on the fact that Rule 10b-5 limitations periods adopted from the forum states, when coupled with the federal equitable tolling doctrine, generally are longer than the periods for express civil liabilities under the 1933 Act in concluding that Rule 10b-5 actions and the express civil liability sections of the 1933 Act are not mutually exclusive. The Court reasoned that because the elements of a Rule 10b-5 claim impose a significantly greater burden on the plaintiff than the express civil liability sections, and because the scope of liability under 10b-5 is more expansive than the relatively limited express rights of action, and because the limitations period for Rule 10b-5 actions accordingly is longer than for such express provisions, plaintiffs should be permitted to join claims for violation of Rule 10b-5 with claims for violations of the 1933 Act.[28]

Albeit it in footnotes, this Court has twice stated not only that courts should look to the most analogous state limitations period in Rule 10b-5 cases, but that the limitations period for 10b-5 actions is longer than the one-year/three-years limitation period urged by the Petitioner.

2. Data Access *Conflicts With This Court's Rulings on Equitable Tolling*

The one-year/three-years limitation provision suggested by the Petitioner also conflicts with decisions of this Court applying federal doctrines of equitable tolling and equitable estoppel. These deeply rooted doctrines hold that it is against equity and good con-

[28]Using the same analysis, courts noting the distinctions between Sections 9 and 18 of the 1934 Act and Rule 10b-5 have permitted 10b-5 actions to proceed even though Sections 9 or 18 would have provided an express remedy. See, e.g., *Chemetron Corp. v. Business Funds, Inc.*, 718 F.2d 725, 727-28 (5th Cir. 1983) (overlap with § 9(a)(4)); *Ross v. A.H. Robins Co.*, 607 F.2d 545, 555 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980) (overlap with § 18(a)). See 5 Jacobs, *Litigation and Practice Under Rule 10b-5* § 11.02 n. 33 (2d ed. 1990 revision).

science to permit a person to profit by his own wrongdoing. Adoption of a statute of repose such as that created in *Data Access* would permit swindlers to profit by trickery and deliberate concealment of their wrongdoing.

In *Holmberg v. Armbrecht*, 327 U.S. 392 (1946), the Court held:

> [F]raudulent conduct on the part of the defendant may have prevented the plaintiff from being diligent and may make it unfair to bar appeal to equity because of mere lapse of time. Equity will not lend itself to such fraud and historically has relieved from it. . . . [W]here a plaintiff has been injured by fraud and "remains in ignorance of it and without any fault or want of diligence or care on his part, the bar of the statute does not begin to run until the fraud is discovered, . . . "
>
> *This equitable doctrine is read into every federal statute of limitation.*

327 U.S. at 396-97 (citations omitted; emphasis added).[29]

It is significant that the opinions of this Court relied upon by the Petitioner — *Agency Holding* and *DelCostello* — did not borrow federal statutes containing a statute of repose.[30] Further, Congress has acquiesced in this practice for many years. Over the last several decades federal courts have agreed that although the court should borrow the state-law limitations periods, the issue of when the period begins to run is governed by the federal law of equitable toll-

[29]This doctrine is not limited to suits in equity. *Bailey v. Glover*, 88 U.S. (21 Wall.) 342, 349 (1874).

[30]In *Agency Holding*, the Court applied the four year statute contained in the Clayton Act, 15 U.S.C. § 15b, to actions under RICO. That limitations provision does not contain a statute of repose; in fact, the lower courts have held that the four year limitations period applied to RICO actions starts to run only when the plaintiff should reasonably have discovered the fraudulent scheme. See, e.g., *Bankers Trust Co. v. Rhoades*, 859 F.2d 1096 (2d Cir. 1988); *Pocahontas Supreme Coal Co. v. Bethlehem Steel Corp.*, 828 F.2d 211 (4th Cir. 1987). The movants' position thus creates an additional anomaly in that under their view Congress intended to cut off 10b-5 actions after three years, whereas it is now generally held that supposedly stale 10b-5 claims may be revived under the guise of a RICO action.

ing.[31] BIA urges the Court not to approve any judicially crafted limitations period for 10b-5 actions that includes a statute of repose.[32]

B. *Resort to State Law Remains the Norm for Borrowing of Limitations Periods*

The Court has adhered to the time-honored practice of borrowing state limitations periods in all but the most unusual cases. Nothing about Rule 10b-5 actions justifies a departure from this procedure. This Court described the practice as "well settled" in *McCluny v. Silliman*, 28 U.S. (3 Pet.) 270, 276-77 (1830). See also *Campbell v. City of Haverhill*, 155 U.S. 610, 616 (1895). The Court in *Holmberg v. Armbrecht*, 327 U.S. 392, 395 (1946) again recognized the validity of the process, and also held that this absorption does not preclude a federal court from also applying the federal doctrine of equitable tolling.

[31]See, e.g., *Gaudin v. KDI Corp.*, 576 F.2d 708, 712 (6th Cir. 1978); *Durham v. Business Management Assoc.*, 847 F.2d 1505, 1508 (11th Cir. 1988); *Semegen v. Weidner*, 780 F.2d 727, 733 (9th Cir. 1985); *Suslick v. Rothschild*, 741 F.2d 1000, 1004 (7th Cir. 1984); *Summer v. Land & Leisure, Inc.*, 664 F.2d 965, 968 (5th Cir. 1981); *Ohio v. Peterson, Lowry, Rall, Barber & Ross*, 651 F.2d 687, 691-92 (10th Cir.), *cert. denied*, 454 U.S. 895 (1981); *IIT v. Cornfeld*, 619 F.2d 909, 929 (2d Cir. 1980); *Cook v. Avien, Inc.*, 573 F.2d 685, 694 (1st Cir. 1978); *Vanderboom v. Sexton*, 422 F.2d 1233, 1240 (8th Cir. 1970), *cert. denied*, 400 U.S. 852 (1970).

[32]A further issue that is presented if this Court adopts some form of a statute of repose for 10b-5 actions is whether the doctrine of equitable estoppel may be applicable. This Court has consistently held that a defendant may be estopped to plead the statute of limitations where his conduct has induced the plaintiff to refrain from filing suit and where the defendant's assurances have lulled the plaintiff into a false sense of security. E.g., *Schroeder v. Young*, 161 U.S. 334 (1896); *Glus v. Brooklyn Eastern District Terminal*, 359 U.S. 231, 232-33 (1959). This principle of equitable estoppel has on occasion been applied to the one-year/three-years limitation period in § 13 of the 1933 Act. See *Katz v. Amos Treat & Co.*, 411 F.2d 1046, 1055 (2d Cir. 1969); *Dyer v. Eastern Trust & Banking Co.*, 336 F.Supp. 890 (N.D. Me. 1971) (§ 12(1)); *Eaton v. Coal Par of West Virginia, Inc.*, [1983-84 Transfer Binder] Fed.Sec.L.Rep. (CCH) ¶ 99,675 (S.D. Fla. 1984) (§ 12(1)). BIA agrees with these courts which have applied the doctrine of equitable estoppel to § 13 limitations periods, and believes that if this Court adopts a statute of repose similar to § 13, assuming it applies the new limitations period retroactively, it should remand the case to the trial court to determine the applicability of the equitable estoppel doctrine. See Joint Appendix, at 40-41, 146-47, and 250-51 for Respondents' allegations of fraudulent concealment justifying equitable estoppel.

More recently, in *Auto Workers v. Hoosier Cardinal Corp.*, 383 U.S. 696 (1966), the Court held that a union's suit against an employer for breach of a collective bargaining agreement under § 301 of the Labor Management Relations Act, 29 U.S.C. § 185, which contains no statute of limitations, was properly governed by the Indiana six-year statute for actions on unwritten contracts. The Court rejected the argument that the action should be governed by the six-month limitations provision governing unfair labor practice proceedings, 29 U.S.C. § 160(b).

In the two cases principally relied on by the Petitioner, *DelCostello v. Teamsters*, 462 U.S. 151 (1983) and *Agency Holding Corp. v. Malley-Duff & Associates, Inc.*, 483 U.S. 143 (1987), the Court adopted a federal limitations period only as an exception to the general rule, and in both instances, it extended the limitations period rather than shortened it.

DelCostello involved a labor relations claim, but unlike *Hoosier*, it was a "hybrid" action involving breach of a collective bargaining agreement by the employer and breach of a duty of fair representation by a union. It was therefore consistent with traditional borrowing practices to look to federal law for a limitations period due to the unique situation presented by two separate forms of action being brought as a "hybrid" claim. If the Court had insisted upon borrowing a state law claim, it would have had to look to the different forms of action making up the hybrid claim, and the limitations periods for those two separate forms of action adopted from state law could vary significantly.[33]

The Court's decision to adopt a federal limitations period for RICO actions in *Agency Holding* was similarly appropriate due to the unique nature of civil RICO actions. Whereas the Court in *DelCostello* faced the task of finding one appropriate limitations period for a hybridized cause of action, in *Agency Holding*, it had to find a limitations period for a mongrel. The basis of a civil RICO violation is a pattern of commissions of various "predicate acts."

[33]Further, the Court found that the more analogous state law limitations provision would be a 30-day limitations period applicable to actions to set aside arbitration awards. The Court rejected such a short limitations period because it was too short to promote the federal policies at stake.

18 U.S.C § 1964(c). Each predicate act may consist of a violation of any number of federal or state law criminal violations. Absent one uniform federal limitations period, the trial court could be faced with the unenviable task of applying as many different state limitations periods as there were alleged predicate acts.

Because of those circumstances peculiar to RICO actions, the Court in *Agency Holding* held that the four-year statute of limitations under the Clayton Act, 15 U.S.C. § 15b, applied to all civil cases under RICO. The Court held that the Clayton Act provided the *closest* analogy to civil RICO not only because of the statutes' similarity in purpose and structure, including the similarity of the elements of the claims, compare 15 U.S.C. §15(a) with 18 U.S.C. §1964(c), but because the RICO cause of action was modeled directly upon the Clayton Act. 483 U.S. at 152. Moreover, the Court specifically observed that because a RICO action is premised on a pattern of widely varying predicate acts, each of which may be analogous to a state law claim having a different limitations period, "there is no comparable single state law analogue to RICO." *Id.*

The Petitioner is wrong in its contention that this Court took some bold step in *Agency Holding* and invited courts to discard the traditional practice of applying state law limitations periods. In *Reed v. United Transportation Union*, 488 U.S. 319 (1989), the Court's most recent pronouncement on the issue, this Court held that claims by a union member under § 101(a)(2) of the Labor Management Reporting and Disclosure Act, 29 U.S.C. § 411(a)(2), alleging that the union violated its members' free speech rights, are governed by the forum state's general or residual personal injury statute of limitation. Despite the same potential for a lack of uniformity engendered by adopting state limitations periods, the Court reasoned that because such claims were "readily analogized" to state personal injury actions, resort to federal law was unnecessary. The *Reed* Court reiterated that *DelCostello* recognized only "a closely circumscribed exception to the general rule that statutes of limitations are to be borrowed from state law." 488 U.S. at 324.

To abandon the traditional rule in this case would allow the exception to swallow up the rule. The first published opinion in which a federal court adopted a state limitations period for a 10b-5 action

was forty-one years ago in *Osborne v. Mallory*, 86 F.Supp. 869 (S.D.N.Y. 1949). Prior to *Data Access*, all twelve circuits which hear federal securities cases had upheld the practice. See Guin & Donaldson, at 547, 574. As discussed above, this Court recognized and relied upon the practice of borrowing state law limitations periods in developing the law of 10b-5. During the four decades since *Osborne*, Congress has made no effort to "correct" this area of the law, thereby indicating its acquiescence in the 10b-5 decisions of the lower courts over a period of several decades. As this Court noted in *Agency Holding*, "we can generally assume that Congress intends by its silence that we borrow state law." 483 U.S. at 147. *Cf. Basic, Inc. v. Levinson*, 485 U.S. 224, 230-31 (1988) (observing that "judicial interpretation and application, *legislative acquiescence*, and the passage of time have removed any doubt that a private cause of action exists for a violation of § 10(b) and Rule 10b-5") (emphasis added). This Court in *Huddleston* also recognized Congress' acquiescence in, and interpreted approval of, the substantial body of 10b-5 case law that had developed prior to *Data Access*:

> In light of this well-established judicial interpretation, Congress' decision to leave § 10(b) intact suggests that Congress ratified the cumulative nature of the § 10(b) action. See *Merrill Lynch, Pierce, Fenner & Smith v. Curran*, 456 U.S. 353, 381-82 (1982). . . .

459 U.S. at 385-86. The same can be said of the traditional practice of adopting state limitations periods: in light of this well-established judicial interpretation over the course of more than four decades, Congress' decision to leave the limitations period for 10b-5 actions intact suggests that Congress has ratified the practice.[34] As elsewhere stated by this Court,

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[34]This congressional acquiescence in the adoption of state limitations periods for 10b-5 actions is particularly persuasive in light of the fact that in 1975, Congress "comprehensively revised the securities laws" and enacted the "'most substantial and significant revision of this country's Federal securities laws since the passage of the Securities Exchange Act in 1934.'" *Huddleston*, 459 U.S. at 384-85 (citation omitted). Those revisions did not include a statute of limitations for 10b-5 actions despite prior pleas for reform.

> [S]tate statutes have repeatedly supplied the periods of limitations for federal causes of action when federal legislation has been silent on the question . . . . *Yet when Congress has disagreed with such an interpretation of its silence*, it has spoken to overturn it by enacting a uniform period of limitations. . . . Against this background, we cannot take the omission in the present statute as a license to judicially devise a uniform time limitation for §301 suits.

Auto Workers v. Hoosier Cardinal Corp., 383 U.S. 696, 704 (1966)(emphasis added). Neither should this court take judicial license to amend Section 10(b) and Rule 10b-5.

C. *Claims Under Rule 10b-5 Do Not Fall Within the DelCostello Exception for Utilizing Federal Limitations Periods*

1. *Rule 10b-5 Limitations Periods Should Be Determined on a Statute-by-Statute Basis*

The first step of the *DelCostello*-exception analysis is to determine "whether all claims arising out of the federal statute 'should be characterized in the same way, or whether they should be evaluated differently depending upon the varying factual circumstances and legal theories presented in each individual case.'" *Agency Holding*, 483 U.S. at 147. Rule 10b-5 claims should be analogized to state law for limitations purposes on a statute-by-statute basis rather than a claim-by-claim basis. See *Wilson v. Garcia*, 471 U.S. 261, 269-70 (1985) and *Owens v. Okure*, 488 U.S. 235 (1989) (holding that the general or residual personal injury statute of limitations of the forum state should always be adopted for civil rights actions under 42 U.S.C. § 1983).

It would be anomalous, for example, to adopt a two-year limitations period for actions by buyers by analogizing to state blue sky law, but to adopt a four-year limitation period for sellers by analogy to a common-law fraud limitations period. See *Friedlander v. Troutman, Sanders, Lockerman and Ashmore*, 788 F.2d 1500, 1504 (11th Cir. 1986) (Adopting the *Wilson* rationale in a 10b-5 action and adopting the forum state blue sky limitations period for all 10b-5 actions, whether asserted by buyers or sellers).

Adoption of 10b-5 limitations periods on a statute-by- statute basis comports with this Court's rulings in *Wilson, Owens*, and *Reed v. United Transp. Union*, 488 U.S. 319, 325-26 (1989). This Court need not throw the baby out with the wash to achieve uniformity. As in those cases, adoption of state limitations periods on a statute-by-statute basis will remove the collateral litigation regarding the appropriate limitations period for each case without taking the drastic step of adopting a federal limitations period, such as that suggested by Petitioner, which was developed to further purposes different from those of 10b-5.[35]

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[35]Contrary to the Petitioner's assertions, the Eleventh Circuit adopted that formulation after *DelCostello* and that court reaffirmed the rule last year by denying review of it *en banc*. See *Smith v. Duff & Phelps*, 891 F.2d 1567, 1570 (11th Cir.), *rehearing en banc denied*, 904 F.2d 712 (11th Cir. 1990). Nor has *Data Access* been as universally lauded as the Petitioner suggests. See, e.g., *Bath v. Bushkin, Gaims, Gaines & Jonas*, 913 F.2d 817 (10th Cir. 1990) (rejecting *Data Access*); *Nesbit v. McNeil*, 896 F.2d 380, 384 (9th Cir. 1990) (same). The Fifth Circuit in *Jensen v. Snellings*, 841 F.2d 600, 606 (5th Cir. 1988) rejected an argument premised on *Agency Holding* that the limitations period for 10b-5 actions should be based on the one-year/three-years rule of § 29 of the 1934 Act, and instead adopted the forum state's limitation period for blue sky claims. The Sixth Circuit has twice rejected the same analysis utilized by the Third Circuit in *Data Access* because of the need for a longer, versus a shorter, limitations period in 10b-5 actions and because of this Court's reliance in *Hochfelder* on the fact that limitations periods for 10b-5 actions generally are longer than those for the express rights of action in the 1933 and 1934 Acts. See *IDS Progressive Fund, Inc. v. First of Michigan*, 533 F.2d 340, 342 (6th Cir. 1976) and *Nickels v. Koehler Management Corp.*, 541 F.2d 611, 614-15 (6th Cir. 1976), *cert. denied*, 429 U.S. 1074 (1977). See also *Roney & Co. v. Goren*, 875 F.2d 1218 (6th Cir. 1989) (noting that the law for 10b-5 actions in the Sixth Circuit is to adopt the most closely analogous limitations period of the forum state, though recognizing the Third Circuit's contrary position). See also *In re Professional Financial Management, Ltd.*, 703 F.Supp. 1388, 1392-93 (D. Minn. 1989) ("The reasoning stated in *Agency Holding Corp. v. Malley-Duff* does not compel the same outcome for § 10(b) and Rule 10b-5 claims as for those under RICO."); *In re Atlantic Financial Mgt. Inc. Sec. Litigation*, 718 F.Supp. 1003, 1010 (D. Mass. 1988) ("The reason that the Court made an exception for civil RICO claims is the variety of substantive predicate offenses which can underlie such actions. This is not the case with section 10(b) and Rule 10b-5 actions, which are all based on violations of securities laws.") (citation omitted).

2. *The Suggested Federal Alternatives Do Not Provide A Closer Analogy Than State Law to Rule 10b-5 Actions*

Although 10b-5 actions satisfy the first branch of the *DelCostello* test in that 10b-5 claims generally should be treated in the same manner, the second and third tests are failed. The second branch of the *DelCostello* exception for resort to federal instead of state law requires that a "rule from elsewhere in federal law clearly provides a *closer* analogy than available state statutes." 462 U.S. at 172 (emphasis added). Petitioner asks the Court to adopt the "one-year/three-year limitations period in the 1933 and 1934 Acts" for all Rule 10b-5 actions. (Petitioner's Brief, at 10.) The Petitioner incorrectly assumes, as did the *Data Access, Short*,[36] and *Ceres*[37] courts, that the statutes of limitation applicable to the express causes of action in the 1933 and 1934 Acts are identical. Although those three circuits all purport to adopt a general one-year/three-years limitation period, each circuit's formulation of that one- year/three-years period differs markedly. See Guin & Donaldson, at 563-65; SEC Amicus Brief, at 26-29. More importantly, the striking differences between Rule 10b-5 and the express causes of action in the 1933 and 1934 Acts to which those limitations periods apply undercut the Petitioner's position.

The causes of action relied upon by Petitioner in the 1933 and 1934 Acts are no more analogous to Rule 10b-5 than blue sky law causes of action. Both the Petitioner and Respondent Comdisco, Inc. argued, for example, that blue sky laws can be distinguished from 10b-5 on the grounds that some blue sky laws protect only purchasers and not sellers and that some provide causes of action against only sellers and not aiders and abettors. (Petitioner's Brief, at 22; Respondent Comdisco's brief, at 23). The same can be said of §§ 11 and 12 of the 1933 Act, on which Petitioner relies. Indeed, the civil liability provision of the Uniform Securities Act, § 410, Unif. Sec. Act (1958), which has been adopted by most states,[38] is based on and is virtually identical to § 12 of the 1933 Act.

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[36]*Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990) (petition for cert. pending).

[37]*Ceres Partners v. GEL Assoc.*, 918 F.2d 349 (2d Cir. 1990).

[38]1 CCH Blue Sky L. Rptr. ¶ 5500.

Nor are the 1933 Act causes of action as similar to Rule 10b-5 as the Petitioner suggests. The express rights of action found in §§ 11 and 12 of the 1933 Act are either strict liability or negligence-based actions. See *Herman & MacLean v. Huddleston*, 459 U.S. 375, 381-84 (1985). Unlike 10b-5 claims, the 1933 Act claims require no proof of reliance, scienter, causation, or even damages. Even the burden of proving negligence, or the lack thereof, is shifted to the defendant. *Id.* Moreover, neither § 11 nor § 12 is applicable to claims by purchasers of tax-exempt municipal bonds.[39] The Seventh Circuit in *Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385 (7th Cir. 1990), *petition for cert. filed.*, 59 U.S.L.W. 3278 (U.S. September 26, 1990)(No. 90-526) premised its analysis on purported analogies between Rule 10b-5 and § 12(2) claims. That court completely ignored the different proof requirements under the two sections that are critical to the statutes of limitation issue, as well as the inapplicability of § 12(2) to many securities and potential defendants in 10b-5 actions.[40]

The *Ceres* and *Data Access* courts purported to premise their analyses on a comparison of Rule 10b-5 with the rights of action found in the 1934, rather than the 1933, Act,[41] but those rights of action also differ significantly from 10b-5 actions. Section 9 of the 1934 Act is unlike the catch-all Rule 10b-5, which is aimed at curbing new and innovative manipulative devices and schemes not explicitly addressed in the 1933 and 1934 Acts. (See Petitioner's Brief, at 6.) Instead, § 9 is "expressly and unambiguously directed toward a narrow species of cases," (see Petitioner's Brief, at 43, distinguishing the five-year limitations period of ITSFEA), and ap-

[39]Sections 11 and 12(1) apply only to securities for which a registration statement was or should have been filed, and municipal bonds are exempt from such filing requirements. Section 12(2) expressly excludes tax-exempt bond issues from its purview.

[40]The Court noted these distinctions in the *Hochfelder* and *Huddleston* cases. See also *Blue Chip Stamps v. Manor Drug Stores*, 421 U.S. 723, 730 n. 4 (1975)(referring to the "contrast between the provisions of Rule 10b-5 and the numerous carefully drawn express civil remedies provided in the acts of both 1933 and 1934").

[41]The Third Circuit in *Data Access* purported to adopt a general one-year/three-year rule found in both the 1933 and 1934 Acts, but now has retreated from that position and contends that its new limitations period is based solely on provisions of the 1934 Act. *Gruber v. Price Waterhouse*, 911 F.2d 960, 964 n. 4 (1990).

plies only to securities registered on a national exchange (and therefore is inapplicable to the securities at issue in this case, or to municipal bonds), and in fact, applies primarily only to a series of six precisely defined forms of securities price manipulations on national exchanges. See § 9(a)(1) through (6). Section § 9 does not appear to impose a reliance requirement and the cause of action may for the most part be asserted only against brokers or dealers who deal directly with the plaintiff. Further, unlike 10b-5 actions, the § 9 cause of action focuses narrowly "upon the amount actually paid by an investor for stock that had been the subject of manipulative activity." *Piper v. Chris-Craft Indus. Inc.*, 430 U.S. 1, 46 (1977).[42]

The only securities to which § 9 is applicable are subject to the reporting requirements of the Exchange Act. See § 9(f). The companies whose securities are subject to § 9 must file annual and quarterly reports (Forms 10-K and 10-Q) with the SEC and must provide similar information directly to shareholders and to the market. Their officers, directors and major shareholders also must file reports with the SEC under § 16 whenever they trade in securities of the company, and the company is required to file with the SEC a report (Form 8-K) disclosing any particularly material events with respect to the company's business. Audited financial statements are required to be filed and delivered to shareholders in those reports.[43]

[42]As Professor Loss has noted, the right of action under § 9(e) "has been a dead letter so far as producing recoveries has been concerned." L. Loss, *Fundamentals of Securities Regulation* 920 (2d ed. 1988).

[43]Such companies also may be subject to the reporting requirements of any exchange on which their securities are traded. The following stock exchange rules are illustrative:

> A corporation whose securities are listed on the New York Stock Exchange, Inc. is expected to release quickly to the public any news or information which might reasonably be expected to materially affect the market for those securities.

New York Stock Exchange Company Manual, A-18 and § 202.05 (1983).

> A listed company is required to make immediate public disclosure of all material information concerning its affairs except in exceptional circumstances.

American Stock Exchange Guide, 101 and § 401 (1983).

Under NASD rules, the securities of an issuer may be refused quotation in the market if the issuer does not "promptly ... disclose to the public through the press

With all that information being disseminated to the market, discovery of facts constituting possible fraud can be more easy than typical securities which are not subject to such stringent reporting rules. Similarly, claims under § 18(a) of the 1934 Act apply only to false or misleading reports filed with the SEC (which, again, is inapplicable here, or to municipal bonds). Like the 1933 Act claims, § 18 does not require proof of scienter and the burden is shifted to the defendant to prove that he acted in good faith.

These distinctions also undercut the Petitioner's arguments based upon the legislative history of the 1934 Act. In anticipation of the argument that many frauds cannot be discovered within the short limitations period it urges this Court to adopt, the Petitioner argues that Congress considered and rejected a longer statute of limitations. Petitioner's brief at 37-42. Petitioner quotes a statement by a Senator Barkley that it would be "manifestly unfair . . . to limit any damaged party to 1 year or 2 years or 3 years in the bringing of a suit, because it may sometimes take 4 or 5 years to discover that a fraud has been committed . . . " Petitioner's brief at 40, note 58, quoting 78 Cong.Rec. 8201 (1934)(Statement of Senator Barkley of Kentucky). Petitioner then argues that the Senate rejected Senator Barkley's argument, but it does not point out the basis of the rejection. In response to Senator Barkley's concern, Senator Austin stated:

> I inquire of the Senator from Kentucky whether he does not recognize another exceptional circumstance in that the burden on proof is shifted around on the question of knowledge or willfulness in a misrepresentation. The committee have put the burden on the defendant, so that in this case the plaintiff does not have to spend any time going out and seeking his evidence. All he has to prove is the fact of misrepresentation.

78 Cong.Rec. 8201 (1934).[44] This colloquy indicates that the short

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any material information which may affect the value of its securities or influence investors' decisions." *National Association of Securities Dealers Manual*, Schedule D, Part 11, § (B)(3)(b).

[44]The SEC's brief, and Guin & Donaldson, discuss a number of other distinctions between 10b-5 actions and the express rights of action in the 1933 and 1934 Acts.

limitations periods applicable to some[45] of the express rights of action in the 1933 and 1934 Acts were adopted only because of the limitations placed on those causes of action.

3. *The Federal Policies At Stake and the Practicalities of Litigation Do Not Make Any Alternative Federal Limitations Periods More Appropriate for 10b-5 Actions:*

Rule 10b-5 claims also do not satisfy the third DelCostello requirement for departing from the norm — "when the federal policies at stake and the practicalities of litigation make [the rule from elsewhere in federal law] a significantly more appropriate vehicle for interstitial lawmaking." 462 U.S. at 172. The federal policy at stake in 10b-5 actions is "protection of the investing public and the national economy through the promotion of 'a high standard of business ethics . . . in every facet of the securities industry.' " *Bateman Eichler, Hill Richards, Inc. v. Berner*, 472 U.S. 299, 315 (1985), quoting *SEC v. Capital Gains Research Bureau, Inc.*, 375 U.S. 180, 186-87 (1963). See also, e.g., *Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967) (central purpose to protect investors).

Petitioner has failed to identify any substantial federal interest furthered by a new limitations and repose period. The Third, Second and Seventh Circuits could do no better than to indicate that a short limitations period would help clear their dockets.[46] As to the "practicalities of litigation," the Second, Third and Seventh Circuits bemoan the "lack of uniformity" to which those decisions, ironically, have added. If uniformity is a paramount objective, then a federal limitations period must always be chosen whenever a federal cause of action lacks an express limitations period. The Petitioner and the circuit court decisions it cites accordingly ignore this

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[45]Of course, although the Petitioner purports to urge adoption of the general one-year/three-years schema of the 1933 and 1934 Acts, it ignores the five-year limitation period of § 20A discussed *infra*.

[46]Such overcrowding is not the result of class action securities fraud actions. Filings of securities fraud class actions have dropped by over 50% since the early 1970s. Whereas 305 securities fraud class actions were filed in federal courts in 1974, only 118 were filed in 1989. 12 *Class Action Reports*, at 316 (July-August 1989). BIA submits that the reduction in the filing of securities class actions is not the result of increased honesty in the market place.

Court's decisions in *Wilson v. Garcia*, 471 U.S. 261 (1985) and *Owens v. Okure*, 488 U.S. 235 (1989), which chose state limitations periods for § 1983 civil rights claims over federal alternatives, and *Reed v. United Transportation Union*, 109 S.Ct. 621 (1989), which chose a state limitations period over federal alternatives for union member claims under § 101(a)(2) of the Labor Management Reporting and Disclosure Act. This Court was aware in those cases that by approving the adoption of state limitations periods, there would be some lack of uniformity and some potential for forum shopping,[47] but those interests were outweighed by the objective of providing an effective remedy.

Because of the difficulties of discovering deliberate frauds in our complex securities markets, the practicalities of litigation require a longer, rather than a shorter, limitations period. See, e.g., *IDS Progressive Fund, Inc. v. First of Michigan*, 533 F.2d 340, 344 (6th Cir. 1976); *Berry Petroleum Co. v. Adams & Peck*, 518 F.2d 402, 409 (2d Cir. 1975); *United California Bank v. Salik*, 481 F.2d 1012, 1015 (9th Cir.), *cert. denied*, 414 U.S. 1004 (1973).

III. IF A FEDERAL LIMITATIONS PERIOD IS TO BE ADOPTED, THERE ARE BETTER ALTERNATIVES THAN THOSE SUGGESTED BY THE PETITIONER

If the court creates a new federal limitations period, the court should not attempt to create some new period out of an agglomeration of the various one-year/three-year rules for the older express remedies of the 1933 and 1934 Acts. There are at least two alternative federal limitations periods that would conform to stated congressional policy and better serve the federal interests at stake.

A. *The Five-Year Period for 10b-5 Types of Fraud Conducted by Insiders, Insider Trading and Securities Fraud Enforcement Act of 1988, 15 U.S.C. § 78t-1(a) ("ITSFEA")*

The statute of limitations in § 20A of ITSFEA provides a more appropriate limitations period than that suggested by the Petitioner.

[47]There is no showing in the record that "forum shopping" is a significant problem in 10b-5 cases, and Congress has expressly provided plaintiffs with a choice of venues under § 27 of the 1934 Act.

Section 20A of the 1934 Act was enacted by Congress as part of ITSFEA to expand the scope of 10b-5 actions. The five-year limitations in ITSFEA is the only statement of congressional intent on the issue of what limitations period Congress deems appropriate for at least some forms of 10b-5 cases.

When Congress enacted the one-year/three-years statutes of limitations in 1934 for certain of the express rights of action, it could not have "intended" for that same limitations period to apply to 10b-5 actions since the implied right of action under Section 10(b) did exist at that time. The legislative history of the 1934 Act does not indicate that Congress even considered the possibility of implied actions under § 10(b). See *In re Data Access*, 843 F.2d at 1547.

Congress enacted ITSFEA, on the other hand, against a backdrop of four decades of judicial decisions construing Rule 10b-5. In fact, ITSFEA was enacted with the specific intent of expanding the scope of Rule 10b-5 by overturning cases denying recovery under Rule 10b-5 for insider trading based upon the misappropriation theory.[48] H.R. Rep. No. 910, 100th Cong., 2d Sess., at 26, *reprinted in* 1988 United States Code Cong. and Admin. News, at 6063. ITSFEA's legislative history acknowledges that private 10b-5 claims "have traditionally served as an important supplement to the Commission's enforcement of federal securities laws," H.R. Report No. 910, 100th Cong., 2d Sess. at 26, reprinted in 1988 U.S. Code Cong. & Admin. News 6063, that ITSFEA was intended to broaden the scope of 10b-5, and that Congress intended to give the courts leeway to develop implied private rights of action under 10b-5 "*in an expansive fashion in the future.*" *Id.*, at 27 (emphasis added).

The history of § 20A of ITSFEA also indicates that the express liability provisions of ITSFEA were designed to work hand-in-hand with implied private causes of action under 10b-5. ITSFEA contemplates that various private causes of action for injuries caused by

[48]Those cases generally relied upon this Court's analysis in *Chiarella v. United States*, 445 U.S. 222 (1980).

insider trading should be implied outside the "contemporaneous trader" situation.[49]

In anticipation that the SEC would urge adoption of the five-year ITSFEA rule for other 10b-5 actions as well, the Petitioner has attempted to distinguish 10b-5 claims generally from insider trading claims. Although the Petitioner is correct that ITSFEA applies only in insider trading cases, the same arguments can be made with respect to each of the express causes of action on which the Petitioner relies. If § 20A is an inappropriate choice for adoption because of the distinctions between 10b-5 claims alleging insider trading and 10b-5 cases generally, then *a fortiori*, the alternatives suggested by Petitioner are inappropriate, because the distinctions between 10b-5 and the express rights of action in the 1933 and 1934 Acts are even greater. Although insider trading is but one variety of a 10b-5 violation, it is nonetheless a 10b-5 violation.[50]

Moreover, to assume that Congress intended a longer statute of limitations to apply to § 20A than to garden variety 10b-5 claims defies common sense. Congress recognized that the two causes of action overlap. The House Report accompanying the act pointed out that the *Anheuser-Busch* case discussed above would give rise to

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[49]As an example of an implied cause of action pursuant to Rule 10b-5 in the insider trading concept, the Report points to *Anheuser-Busch Companies, Inc. v. Thayer*, CA3-85-0794-R (N.D. Texas 1986), in which a tipper disclosed the plaintiff's intent to acquire another corporation, thereby pushing up the price of the stock by insider trading and allegedly increasing the tender offer price by $80 million. The Report recognized that Anheuser-Busch, the plaintiff in the case, was not a "contemporaneous trader," for whom an express cause of action would have existed under the 1934 Act under then-existing case law. It concluded, however, that an implied 10b-5 cause of action *should* exist on Anheuser-Busch's behalf but wished to clarify in ITSFEA what sorts of insider trading would constitute a violation of Rule 10b-5. H.R. Report at 28.

[50]Congress enacted ITSFEA in order to extend the breadth of Rule 10b-5 actions to those alleging insider trading based upon the misappropriation theory. Further, unlike § 9 or 18 claims of the 1934 Act, or § 11 or 12 claims of the 1933 Act, the elements of proof for a § 20A action are identical to the elements of any other 10b-5 action. (See SEC Amicus Brief, at 16-17.) Unlike the express rights of action, scienter, causation, and damages all are elements of the cause of action, and the difficulty of discovering insider trading, if anything, is less than the difficulty of discovering financial fraud or other deliberate securities frauds due to the availability to stockholders of information regarding all insiders' purchases and sales of their corporation's securities.

both implied 10b-5 actions and express causes of action under § 20A. Moreover, in considering ITSFEA, Congress took into account the fact that some economists and academics favor legalizing insider trading on the theory that it promotes efficient markets. Report at 7. In addition to such relatively benign activities as insider trading, § 10(b) covers such obviously nefarious practices as Ponzi schemes in which innocent people are cheated out of their life's savings. In light of the fact that some of the same activities are encompassed by both sections and in light of the fact that some 10b-5 claims involve activities far worse that insider trading, it is illogical to assume that Congress intended for insider trading to have a longer statute of limitations than an action that is based on intentional fraud.[51]

B. *The Three-Year Period in a 10b-5 Clone, The Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701, et seq. is also more apposite than the alternatives suggested by the Petitioner.*

A second alternative is found in the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1701 et seq. Section 1703(a)(2)(A),(B) and (C) of that Act as amended in 1979 duplicates the language of Rule 10b-5, except that it applies to the fraudulent interstate sale of resort and other properties rather than to securities. Section 1709(a) of the Act creates a cause of action based upon that 10b-5 clone, and section 1711(a)(2) of the Act establishes a limitations rule of "three years after discovery of the violation or after discovery should have been made by the exercise of reasonable diligence."

This Court has noted that *when originally passed*, the Interstate Land Sales Full Disclosure Act was modeled on the 1933 Act and had disclosure as its central purpose. *Flint Ridge Dev. Co. v. Scenic Rivers Ass'n of Oklahoma*, 426 U.S. 776, 778-79 (1976). But by

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[51]The Seventh Circuit has indicated that the five year ITSFEA rule can be equitably tolled, and BIA agrees with that limited portion of the Seventh Circuit's opinion in *Short v. Belleville Shoe Mfg. Co.*, 908 F.2d 1385, 1391-92 (7th Cir. 1990), *petition for cert. filed.*, 59 U.S.L.W. 3278 (U.S. September 26, 1990)(No. 90-526).

1979, Congress recognized that the statute was not fulfilling its objective, which was to combat extensive fraud in the land sales industry simulating fraud in the sale of securities. Congress noted that as in the securities business, con men offering to sell or lease land were often using sophisticated sales teams who would promise that the land (which was under water or suitable only for grazing) "was a good investment" and "easily resalable." H.R. Report No. 96-154, 96th Cong., 1st Sess. 30, reprinted in 3 U.S. Code Cong. & Admin. News 2346. Because Congress found that the original formulation of the act, which included a three-year statute of repose, was largely ineffectual, it amended the Act in 1979 "to conform more closely to the language of the securities laws," particularly Rule 10b-5, and significantly, Congress removed the three-year absolute limitation and increased the limitations period to three years from discovery. *Id.*, at 34-35, reprinted in 1979 U.S. Code Cong. & Admin. News 2350. Because the 10b-5 cause of action in the Interstate Land Sales Full Disclosure Act is identical to, and has the same elements and burdens of proof as, and the same goals as, Rule 10b-5, that cause of action provides as close an analogy to Rule 10b-5 actions as is imaginable.

CONCLUSION

This Court should adhere to its statement in *DelCostello* that "resort to state law remains the norm for borrowing of limitations periods," 462 U.S. at 171, and rule that federal courts must adopt the limitations period from the forum state's laws for securities fraud, and that such borrowed time period should start to run only after discovery of the violation or after discovery should have been made by the exercise of reasonable diligence. If a federal limitations period is adopted, the Court should adopt a limitations period that is subject to tolling in order to promote enforcement of the 1934 Act. BIA suggests that the Court adopt the five year limitations period of § 20A of the 1934 Act, coupled with equitable tolling, or the three-years from discovery limitations period of the Interstate Land Sales Full Disclosure Act.

Respectfully submitted,

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